

File No. PCAOB 2009-02
Consists of 682 Pages

SECURITIES AND EXCHANGE COMMISSION

Washington, DC 20549

Form 19b-4

Proposed Rules

By

Public Company Accounting Oversight Board

SEC
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Section

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In accordance with Rule 19b-4 under the
Securities Exchange Act of 1934

1. Text of the Proposed Rules

(a) Pursuant to the provisions of Section 107(b) of the Sarbanes-Oxley Act of 2002 (the "Act"), the Public Company Accounting Oversight Board (the "Board" or the "PCAOB") is filing with the Securities and Exchange Commission ("SEC" or "Commission") proposed rules, Auditing Standard No. 7, *Engagement Quality Reviewer* ("Auditing Standard No. 7"); and conforming amendment to the Board's interim quality control standards. The proposed rules are attached as Exhibit A to this rule filing.

(b) Auditing Standard No. 7 would supersede the Securities and Exchange Commission Practice Section ("SECPS") of the American Institute of Certified Public Accountants ("AICPA") Requirements of Membership Section 1000.08(f), the Board's interim concurring partner review requirement that the Board adopted on April 16, 2003, as part of its interim quality control standards.

(c) Not applicable.

2. Procedures of the Board

(a) The Board approved the proposed rules, and authorized them for filing with the SEC, at its Open Meeting on July 28, 2009. No other action by the Board is necessary for the filing of the proposed rules.

(b) Questions regarding this rule filing may be directed to Gregory Scates, Deputy Chief Auditor (202-207-9114; scatesg@pcaobus.org), Dima Andriyenko, Associate Chief Auditor (202-207-9130; andriyenkod@pcaobus.org), or Nina Mojiri-Azad, Assistant General Counsel (202-207-9035; mojiriazadn@pcaobus.org).

3. Board's Statement of the Purpose of, and the Statutory Basis for, the Proposed Rules Change

(a) Purpose

Section 103 of the Sarbanes-Oxley Act (the "Act") directs the Board, among other things, to set standards for public company audits, including a requirement for each registered public accounting firm to "provide a concurring or second partner review and approval of [each] audit report (and other related information), and concurring approval in its issuance"

As discussed more fully in Exhibit 3, the Board adopted Auditing Standard No. 7 because it believed that a well-performed engagement quality review ("EQR") can serve as an important safeguard against erroneous or insufficiently supported audit opinions and, accordingly, can contribute to audit quality. The proposed rules are intended to enhance the quality of the EQR by strengthening the existing requirements. Auditing Standard No. 7 provides for a rigorous review that will serve as a meaningful check on the work performed by the engagement team and, the Board believes, should increase the likelihood that a registered public accounting firm will catch any significant engagement deficiencies before it issues its audit report. As a result, the Board recognizes that more work may be necessary under Auditing Standard No. 7 than was performed in some concurring reviews under the existing requirements.

Auditing Standard No. 7 requires the engagement quality reviewer (or the "reviewer") to evaluate the significant judgments made and related conclusions reached by the engagement team in forming the overall conclusion on the engagement and in preparing the engagement report. Auditing Standard No. 7

also requires the engagement quality reviewer to perform certain procedures designed to focus the reviewer on those judgments and conclusions. The procedures required of the reviewer by Auditing Standard No. 7 are different in nature from the procedures required of the engagement team. Unlike the engagement team, a reviewer does not perform substantive procedures or obtain sufficient evidence to support an opinion on the financial statements or internal control over financial reporting. If more audit work is necessary before the reviewer may provide concurring approval of issuance, the engagement team – not the reviewer – is responsible under PCAOB standards for performing the work. In contrast, the reviewer fulfills his or her responsibility to perform an effective review of the engagement under the EQR standard by holding discussions with the engagement team, reviewing documentation, and determining whether he or she can provide concurring approval of issuance.

The proposed rules also amend the Board's interim quality control standards by replacing the third sentence of paragraph .18 of in QC section 20, "System of Quality Control for a CPA Firm's Accounting and Auditing Practice" with a statement indicating that these policies and procedures also should address engagement quality reviews pursuant to PCAOB Auditing Standard No. 7.

(b) Statutory Basis

The statutory basis for the proposed rules is Title I of the Act.

4. Board's Statement on Burden on Competition

The Board does not believe that the proposed rules will result in any burden on competition that is not necessary or appropriate in furtherance of the purposes of the Act. The proposed rule changes would apply equally to all registered public accounting firms.

5. Board's Statement on Comments on the Proposed Rules Change Received from Members, Participants or Others

The Board initially released the proposed rules for public comment on February 26, 2008. See Exhibit 2(a)(A). The Board received 38 written comment letters relating to its initial proposed rules. See Exhibits 2(a)(B) and 2(a)(C). The Board considered these comments and made significant changes to the initial proposed rules. As a result, the Board again sought public comment on the proposed rules on March 4, 2009. See Exhibit 2(a)(D). The Board received 30 written comment letters relating to its reproposal of the proposed rules. See Exhibits 2(a)(E) and 2(a)(F).

The Board has carefully considered all comments it has received. In response to the written comments received on both the initial and reproposal of the proposed rules, the Board has clarified and modified certain aspects of the proposed rules. The Board's response to the comments it received and the changes made to the rules in response to the comments received are summarized in Exhibits 2(a)(D) and 3 to this filing.

6. Extension of Time Period for Commission Action

The Board does not consent to an extension of the time period specified in Section 19(b)(2) of the Securities Exchange Act of 1934.

7. Basis for Summary Effectiveness Pursuant to Section 19(b)(3) or for Accelerated Effectiveness Pursuant to Section 19(b)(2)

Not applicable.

8. Proposed Rules Based on Rules of Another Board or of the Commission

Not applicable.

9. Exhibits

Exhibit A – Text of the Proposed Rules

Exhibit 1 – Form of Notice of Proposed Rules for Publication in the Federal Register.

Exhibit 2(a)(A) – PCAOB Release No. 2008-002 (February 26, 2008)

Exhibit 2(a)(B) – Alphabetical List of Comments on the rules proposed in PCAOB Release No 2008-002

Exhibit 2(a)(C) – Written comments on the rules proposed in PCAOB Release No. 2008-002

Exhibit 2(a)(D) – PCAOB Release No. 2009-001 (March 4, 2009)

Exhibit 2(a)(E) – Alphabetical List of Comments on the rules proposed in PCAOB Release No 2009-001

Exhibit 2(a)(F) – Written comments on the rules proposed in PCAOB Release No. 2009-001

Exhibit 2(b) – Transcript of portion of Public Standing Advisory Group meeting concerning the proposed rule change

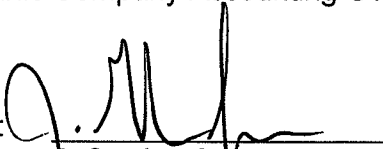
Exhibit 3 – PCAOB Release No. 2009-004 (July 28, 2009)

10. Signatures

Pursuant to the requirements of the Act and the Securities Exchange Act of 1934, as amended, the Board has duly caused this filing to be signed on its behalf by the undersigned thereunto duly authorized.

Public Company Accounting Oversight Board

By:

A handwritten signature in black ink, appearing to read 'J. Gordon Seymour', written over a horizontal line.

J. Gordon Seymour
General Counsel
and Secretary

August 4, 2009

Exhibit A – Text of the Proposed Rules

Language deleted by the proposed rule changes is set forth in brackets. Language that is added is underlined.

Auditing Standard No. 7

Supersedes SECPS Requirements of Membership § 1000.08(f).

Engagement Quality Review

Applicability of Standard

1. An engagement quality review and concurring approval of issuance are required for each audit engagement and for each engagement to review interim financial information conducted pursuant to the standards of the Public Company Accounting Oversight Board ("PCAOB").

Objective

2. The objective of the engagement quality reviewer is to perform an evaluation of the significant judgments made by the engagement team and the related conclusions reached in forming the overall conclusion on the engagement and in preparing the engagement report, if a report is to be issued, in order to determine whether to provide concurring approval of issuance.^{1/}

Qualifications of an Engagement Quality Reviewer

3. The engagement quality reviewer must be an associated person of a registered public accounting firm. An engagement quality reviewer from the firm that issues the engagement report (or communicates an engagement conclusion, if no report is issued) must be a partner or another individual in an equivalent position. The engagement quality reviewer may also be an individual from outside the firm.^{2/}

^{1/} In the context of an audit, "engagement report" refers to the audit report (or reports if, in an integrated audit, the auditor issues separate reports on the financial statements and internal control over financial reporting). In the context of an engagement to review interim financial information, the term refers to the report on interim financial information. An engagement report might not be issued in connection with a review of interim financial information. See paragraph .03 of AU section ("sec.") 722, *Interim Financial Information*.

^{2/} An outside reviewer who is not already associated with a registered public accounting firm would become associated with the firm issuing the report if *he or she* (rather than, or in addition to,

4. As described below, an engagement quality reviewer must have competence, independence, integrity, and objectivity.

Note: The firm's quality control policies and procedures should include provisions to provide the firm with reasonable assurance that the engagement quality reviewer has sufficient competence, independence, integrity, and objectivity to perform the engagement quality review in accordance with the standards of the PCAOB.

Competence

5. The engagement quality reviewer must possess the level of knowledge and competence related to accounting, auditing, and financial reporting required to serve as the engagement partner on the engagement under review.^{3/}

Independence, Integrity, and Objectivity

6. The engagement quality reviewer must be independent of the company, perform the engagement quality review with integrity, and maintain objectivity in performing the review.

Note: The reviewer may use assistants in performing the engagement quality review. Personnel assisting the engagement quality reviewer also must be independent, perform the assigned procedures with integrity, and maintain objectivity in performing the review.

7. To maintain objectivity, the engagement quality reviewer and others who assist the reviewer should not make decisions on behalf of the engagement team or assume any of the responsibilities of the engagement team. The engagement partner remains responsible for the engagement and its performance, notwithstanding the involvement of the engagement quality reviewer and others who assist the reviewer.

8. The person who served as the engagement partner during either of the two audits preceding the audit subject to the engagement quality review may not be the engagement quality reviewer. Registered firms that qualify for the exemption under Rule

his or her firm or other employer): (1) receives compensation from the firm issuing the report for performing the review or (2) performs the review as agent for the firm issuing the report. See PCAOB Rule 1001(p)(i) for the definition of an associated person of a registered public accounting firm.

^{3/} The term "engagement partner" has the same meaning as the phrases "auditor with final responsibility for the audit" in AU sec. 311, *Planning and Supervision*, and "practitioner-in-charge of an engagement" in PCAOB interim quality control standard QC sec. 40, *The Personnel Management Element of a Firm's System of Quality Control-Competencies Required by a Practitioner-in-Charge of an Attest Engagement*. QC sec. 40 describes the competencies required of a practitioner-in-charge of an attest engagement.

2-01(c)(6)(ii) of Regulation S-X, 17 C.F.R. § 210.2-01(c)(6)(ii), are exempt from the requirement in this paragraph.

Engagement Quality Review for an Audit

Engagement Quality Review Process

9. In an audit engagement, the engagement quality reviewer should evaluate the significant judgments made by the engagement team and the related conclusions reached in forming the overall conclusion on the engagement and in preparing the engagement report. To evaluate such judgments and conclusions, the engagement quality reviewer should, to the extent necessary to satisfy the requirements of paragraphs 10 and 11: (1) hold discussions with the engagement partner and other members of the engagement team, and (2) review documentation.

10. In an audit, the engagement quality reviewer should:

- a. Evaluate the significant judgments that relate to engagement planning, including –
 - The consideration of the firm's recent engagement experience with the company and risks identified in connection with the firm's client acceptance and retention process,
 - The consideration of the company's business, recent significant activities, and related financial reporting issues and risks, and
 - The judgments made about materiality and the effect of those judgments on the engagement strategy.
- b. Evaluate the engagement team's assessment of, and audit responses to –
 - Significant risks identified by the engagement team, including fraud risks, and
 - Other significant risks identified by the engagement quality reviewer through performance of the procedures required by this standard.

Note: A *significant risk* is a risk of material misstatement that is important enough to require special audit consideration.

- c. Evaluate the significant judgments made about (1) the materiality and disposition of corrected and uncorrected identified misstatements and (2) the severity and disposition of identified control deficiencies.

- d. Review the engagement team's evaluation of the firm's independence in relation to the engagement.
- e. Review the engagement completion document^{4/} and confirm with the engagement partner that there are no significant unresolved matters.
- f. Review the financial statements, management's report on internal control, and the related engagement report.
- g. Read other information in documents containing the financial statements to be filed with the Securities and Exchange Commission ("SEC")^{5/} and evaluate whether the engagement team has taken appropriate action with respect to any material inconsistencies with the financial statements or material misstatements of fact of which the engagement quality reviewer is aware.
- h. Based on the procedures required by this standard, evaluate whether appropriate consultations have taken place on difficult or contentious matters. Review the documentation, including conclusions, of such consultations.
- i. Based on the procedures required by this standard, evaluate whether appropriate matters have been communicated, or identified for communication, to the audit committee, management, and other parties, such as regulatory bodies.

Evaluation of Engagement Documentation

11. In an audit, the engagement quality reviewer should evaluate whether the engagement documentation that he or she reviewed when performing the procedures required by paragraph 10 –

- a. Indicates that the engagement team responded appropriately to significant risks, and
- b. Supports the conclusions reached by the engagement team with respect to the matters reviewed.

^{4/} Paragraph 13 of PCAOB Auditing Standard No. 3, *Audit Documentation*, requires the auditor to identify all significant findings or issues in an engagement completion document.

^{5/} See paragraphs .04-.06 of AU sec. 550, *Other Information in Documents Containing Audited Financial Statements*; AU sec. 711, *Filings Under Federal Securities Statutes*.

Concurring Approval of Issuance

12. In an audit, the engagement quality reviewer may provide concurring approval of issuance only if, after performing with due professional care^{6/} the review required by this standard, he or she is not aware of a significant engagement deficiency.

Note: A significant engagement deficiency in an audit exists when (1) the engagement team failed to obtain sufficient appropriate evidence in accordance with the standards of the PCAOB, (2) the engagement team reached an inappropriate overall conclusion on the subject matter of the engagement, (3) the engagement report is not appropriate in the circumstances, or (4) the firm is not independent of its client.

13. In an audit, the firm may grant permission to the client to use the engagement report only after the engagement quality reviewer provides concurring approval of issuance.^{7/}

Engagement Quality Review for a Review of Interim Financial Information

Engagement Quality Review Process

14. In an engagement to review interim financial information, the engagement quality reviewer should evaluate the significant judgments made by the engagement team and the related conclusions reached in forming the overall conclusion on the engagement and in preparing the engagement report, if a report is to be issued. To evaluate such judgments and conclusions, the engagement quality reviewer should, to the extent necessary to satisfy the requirements of paragraphs 15 and 16: (1) hold discussions with the engagement partner and other members of the engagement team, and (2) review documentation.

^{6/} See AU sec. 230, *Due Professional Care in the Performance of Work*.

^{7/} Concurring approval of issuance by the engagement quality reviewer also is required when reissuance of an engagement report requires the auditor to update his or her procedures for subsequent events. In that case, the engagement quality reviewer should update the engagement quality review by addressing those matters related to the subsequent events procedures.

15. In a review of interim financial information, the engagement quality reviewer should:

- a. Evaluate the significant judgments that relate to engagement planning, including the consideration of –
 - The firm's recent engagement experience with the company and risks identified in connection with the firm's client acceptance and retention process,
 - The company's business, recent significant activities, and related financial reporting issues and risks, and
 - The nature of identified risks of material misstatement due to fraud.
- b. Evaluate the significant judgments made about (1) the materiality and disposition of corrected and uncorrected identified misstatements and (2) any material modifications that should be made to the disclosures about changes in internal control over financial reporting.
- c. Perform the procedures described in paragraphs 10.d and 10.e.
- d. Review the interim financial information for all periods presented and for the immediately preceding interim period, management's disclosure for the period under review, if any, about changes in internal control over financial reporting, and the related engagement report, if a report is to be issued.
- e. Read other information in documents containing interim financial information to be filed with the SEC^{8/} and evaluate whether the engagement team has taken appropriate action with respect to material inconsistencies with the interim financial information or material misstatements of fact of which the engagement quality reviewer is aware.
- f. Perform the procedures in paragraphs 10.h and 10.i

Evaluation of Engagement Documentation

16. In a review of interim financial information, the engagement quality reviewer should evaluate whether the engagement documentation that he or she reviewed when performing the procedures required by paragraph 15 supports the conclusions reached by the engagement team with respect to the matters reviewed.

^{8/} See AU sec. 722.18f; AU sec. 711.

Concurring Approval of Issuance

17. In a review of interim financial information, the engagement quality reviewer may provide concurring approval of issuance only if, after performing with due professional care the review required by this standard, he or she is not aware of a significant engagement deficiency.

Note: A significant engagement deficiency in a review of interim financial information exists when (1) the engagement team failed to perform interim review procedures necessary in the circumstances of the engagement, (2) the engagement team reached an inappropriate overall conclusion on the subject matter of the engagement, (3) the engagement report is not appropriate in the circumstances, or (4) the firm is not independent of its client.

18. In a review of interim financial information, the firm may grant permission to the client to use the engagement report (or communicate an engagement conclusion to its client, if no report is issued) only after the engagement quality reviewer provides concurring approval of issuance.

Documentation of an Engagement Quality Review

19. Documentation of an engagement quality review should contain sufficient information to enable an experienced auditor, having no previous connection with the engagement, to understand the procedures performed by the engagement quality reviewer, and others who assisted the reviewer, to comply with the provisions of this standard, including information that identifies:

- a. The engagement quality reviewer, and others who assisted the reviewer,
- b. The documents reviewed by the engagement quality reviewer, and others who assisted the reviewer,
- c. The date the engagement quality reviewer provided concurring approval of issuance or, if no concurring approval of issuance was provided, the reasons for not providing the approval.

20. Documentation of an engagement quality review should be included in the engagement documentation.

21. The requirements related to retention of and subsequent changes to audit documentation in PCAOB Auditing Standard No. 3, *Audit Documentation*, apply with respect to the documentation of the engagement quality review.

Conforming Amendment to PCAOB Interim Quality Control Standards

QC sec. 20, "System of Quality Control for a CPA Firm's Accounting and Auditing Practice"

QC section ("sec.") 20, "System of Quality Control for a CPA Firm's Accounting and Auditing Practice" of the Board's interim quality control standards is amended as follows –

The third sentence of paragraph .18 of QC sec. 20 is replaced with the following sentence:

These policies and procedures also should address engagement quality reviews pursuant to PCAOB Auditing Standard No. 7, *Engagement Quality Review*.

EXHIBIT 1

SECURITIES AND EXCHANGE COMMISSION
(Release No. 34- ; File No. PCAOB-2009-02)

[Date]

Public Company Accounting Oversight Board; Notice of Filing of Proposed Rules on Auditing Standard No. 7, Engagement Quality Review, and Conforming Amendment.

Pursuant to Section 107(b) of the Sarbanes-Oxley Act of 2002 (the "Act"), notice is hereby given that on August 4, 2009, the Public Company Accounting Oversight Board (the "Board" or the "PCAOB") filed with the Securities and Exchange Commission (the "Commission") the proposed rules described in items I, II, and III below, which items have been prepared by the Board. The Commission is publishing this notice to solicit comments on the proposed rules from interested persons.

I. Board's Statement of the Terms of Substance of the Proposed Rules

On July 28, 2009, the Board adopted Auditing Standard No. 7, Engagement Quality Review, and an amendment to the Board's Interim Quality Control Standards (collectively, "the proposed rules "). The text of the proposed rules text is set out below. Language that is added by the amendment to the Board's Interim Quality Control Standards is underlined.

Auditing Standard No. 7

Supersedes SECPS Requirements of Membership § 1000.08(f).

Engagement Quality Review

Applicability of Standard

1. An engagement quality review and concurring approval of issuance are required for each audit engagement and for each engagement to review interim financial information conducted pursuant to the standards of the Public Company Accounting Oversight Board ("PCAOB").

Objective

2. The objective of the engagement quality reviewer is to perform an evaluation of the significant judgments made by the engagement team and the related conclusions reached in forming the overall conclusion on the engagement and in preparing the engagement report, if a report is to be issued, in order to determine whether to provide concurring approval of issuance.^{1/}

Qualifications of an Engagement Quality Reviewer

3. The engagement quality reviewer must be an associated person of a registered public accounting firm. An engagement quality reviewer from the firm that issues the engagement report (or communicates an engagement conclusion, if no report is issued) must be a partner or another individual in an equivalent position. The engagement quality reviewer may also be an individual from outside the firm.^{2/}

^{1/} In the context of an audit, "engagement report" refers to the audit report (or reports if, in an integrated audit, the auditor issues separate reports on the financial statements and internal control over financial reporting). In the context of an engagement to review interim financial information, the term refers to the report on interim financial information. An engagement report might not be issued in connection with a review of interim financial information. See paragraph .03 of AU section ("sec.") 722, *Interim Financial Information*.

^{2/} An outside reviewer who is not already associated with a registered public accounting firm would become associated with the firm issuing the report if *he or she* (rather than, or in addition to, his or her firm or other employer): (1) receives compensation from the firm issuing the report for performing the review or (2) performs the review as agent for the firm issuing the report. See PCAOB Rule 1001(p)(i) for the definition of an associated person of a registered public accounting firm.

4. As described below, an engagement quality reviewer must have competence, independence, integrity, and objectivity.

Note: The firm's quality control policies and procedures should include provisions to provide the firm with reasonable assurance that the engagement quality reviewer has sufficient competence, independence, integrity, and objectivity to perform the engagement quality review in accordance with the standards of the PCAOB.

Competence

5. The engagement quality reviewer must possess the level of knowledge and competence related to accounting, auditing, and financial reporting required to serve as the engagement partner on the engagement under review.^{3/}

Independence, Integrity, and Objectivity

6. The engagement quality reviewer must be independent of the company, perform the engagement quality review with integrity, and maintain objectivity in performing the review.

Note: The reviewer may use assistants in performing the engagement quality review. Personnel assisting the engagement quality reviewer also must be independent, perform the assigned procedures with integrity, and maintain objectivity in performing the review.

7. To maintain objectivity, the engagement quality reviewer and others who assist the reviewer should not make decisions on behalf of the engagement team or assume any of the responsibilities of the engagement team. The engagement partner remains responsible for the engagement and its performance, notwithstanding the involvement of the engagement quality reviewer and others who assist the reviewer.

8. The person who served as the engagement partner during either of the two audits preceding the audit subject to the engagement quality review may not be the engagement quality reviewer. Registered firms that qualify for the exemption under Rule 2-01(c)(6)(ii) of Regulation S-X, 17 C.F.R. § 210.2-01(c)(6)(ii), are exempt from the requirement in this paragraph.

^{3/} The term "engagement partner" has the same meaning as the phrases "auditor with final responsibility for the audit" in AU sec. 311, *Planning and Supervision*, and "practitioner-in-charge of an engagement" in PCAOB interim quality control standard QC sec. 40, *The Personnel Management Element of a Firm's System of Quality Control-Competencies Required by a Practitioner-in-Charge of an Attest Engagement*. QC sec. 40 describes the competencies required of a practitioner-in-charge of an attest engagement.

Engagement Quality Review for an Audit

Engagement Quality Review Process

9. In an audit engagement, the engagement quality reviewer should evaluate the significant judgments made by the engagement team and the related conclusions reached in forming the overall conclusion on the engagement and in preparing the engagement report. To evaluate such judgments and conclusions, the engagement quality reviewer should, to the extent necessary to satisfy the requirements of paragraphs 10 and 11: (1) hold discussions with the engagement partner and other members of the engagement team, and (2) review documentation.

10. In an audit, the engagement quality reviewer should:

- a. Evaluate the significant judgments that relate to engagement planning, including –
 - The consideration of the firm's recent engagement experience with the company and risks identified in connection with the firm's client acceptance and retention process,
 - The consideration of the company's business, recent significant activities, and related financial reporting issues and risks, and
 - The judgments made about materiality and the effect of those judgments on the engagement strategy.
- b. Evaluate the engagement team's assessment of, and audit responses to –
 - Significant risks identified by the engagement team, including fraud risks, and
 - Other significant risks identified by the engagement quality reviewer through performance of the procedures required by this standard.

Note: A *significant risk* is a risk of material misstatement that is important enough to require special audit consideration.

- c. Evaluate the significant judgments made about (1) the materiality and disposition of corrected and uncorrected identified misstatements and (2) the severity and disposition of identified control deficiencies.
- d. Review the engagement team's evaluation of the firm's independence in relation to the engagement.

- e. Review the engagement completion document^{4/} and confirm with the engagement partner that there are no significant unresolved matters.
- f. Review the financial statements, management's report on internal control, and the related engagement report.
- g. Read other information in documents containing the financial statements to be filed with the Securities and Exchange Commission ("SEC")^{5/} and evaluate whether the engagement team has taken appropriate action with respect to any material inconsistencies with the financial statements or material misstatements of fact of which the engagement quality reviewer is aware.
- h. Based on the procedures required by this standard, evaluate whether appropriate consultations have taken place on difficult or contentious matters. Review the documentation, including conclusions, of such consultations.
- i. Based on the procedures required by this standard, evaluate whether appropriate matters have been communicated, or identified for communication, to the audit committee, management, and other parties, such as regulatory bodies.

Evaluation of Engagement Documentation

11. In an audit, the engagement quality reviewer should evaluate whether the engagement documentation that he or she reviewed when performing the procedures required by paragraph 10 –

- a. Indicates that the engagement team responded appropriately to significant risks, and
- b. Supports the conclusions reached by the engagement team with respect to the matters reviewed.

^{4/} Paragraph 13 of PCAOB Auditing Standard No. 3, *Audit Documentation*, requires the auditor to identify all significant findings or issues in an engagement completion document.

^{5/} See paragraphs .04-.06 of AU sec. 550, *Other Information in Documents Containing Audited Financial Statements*; AU sec. 711, *Filings Under Federal Securities Statutes*.

Concurring Approval of Issuance

12. In an audit, the engagement quality reviewer may provide concurring approval of issuance only if, after performing with due professional care^{6/} the review required by this standard, he or she is not aware of a significant engagement deficiency.

Note: A *significant engagement deficiency* in an audit exists when (1) the engagement team failed to obtain sufficient appropriate evidence in accordance with the standards of the PCAOB, (2) the engagement team reached an inappropriate overall conclusion on the subject matter of the engagement, (3) the engagement report is not appropriate in the circumstances, or (4) the firm is not independent of its client.

13. In an audit, the firm may grant permission to the client to use the engagement report only after the engagement quality reviewer provides concurring approval of issuance.^{7/}

Engagement Quality Review for a Review of Interim Financial Information

Engagement Quality Review Process

14. In an engagement to review interim financial information, the engagement quality reviewer should evaluate the significant judgments made by the engagement team and the related conclusions reached in forming the overall conclusion on the engagement and in preparing the engagement report, if a report is to be issued. To evaluate such judgments and conclusions, the engagement quality reviewer should, to the extent necessary to satisfy the requirements of paragraphs 15 and 16: (1) hold discussions with the engagement partner and other members of the engagement team, and (2) review documentation.

^{6/} See AU sec. 230, *Due Professional Care in the Performance of Work*.

^{7/} Concurring approval of issuance by the engagement quality reviewer also is required when reissuance of an engagement report requires the auditor to update his or her procedures for subsequent events. In that case, the engagement quality reviewer should update the engagement quality review by addressing those matters related to the subsequent events procedures.

15. In a review of interim financial information, the engagement quality reviewer should:

- a. Evaluate the significant judgments that relate to engagement planning, including the consideration of –
 - The firm's recent engagement experience with the company and risks identified in connection with the firm's client acceptance and retention process,
 - The company's business, recent significant activities, and related financial reporting issues and risks, and
 - The nature of identified risks of material misstatement due to fraud.
- b. Evaluate the significant judgments made about (1) the materiality and disposition of corrected and uncorrected identified misstatements and (2) any material modifications that should be made to the disclosures about changes in internal control over financial reporting.
- c. Perform the procedures described in paragraphs 10.d and 10.e.
- d. Review the interim financial information for all periods presented and for the immediately preceding interim period, management's disclosure for the period under review, if any, about changes in internal control over financial reporting, and the related engagement report, if a report is to be issued.
- e. Read other information in documents containing interim financial information to be filed with the SEC^{8/} and evaluate whether the engagement team has taken appropriate action with respect to material inconsistencies with the interim financial information or material misstatements of fact of which the engagement quality reviewer is aware.
- f. Perform the procedures in paragraphs 10.h and 10.i

Evaluation of Engagement Documentation

16. In a review of interim financial information, the engagement quality reviewer should evaluate whether the engagement documentation that he or she reviewed when performing the procedures required by paragraph 15 supports the conclusions reached by the engagement team with respect to the matters reviewed.

^{8/} See AU sec. 722.18f; AU sec. 711.

Concurring Approval of Issuance

17. In a review of interim financial information, the engagement quality reviewer may provide concurring approval of issuance only if, after performing with due professional care the review required by this standard, he or she is not aware of a significant engagement deficiency.

Note: A *significant engagement deficiency* in a review of interim financial information exists when (1) the engagement team failed to perform interim review procedures necessary in the circumstances of the engagement, (2) the engagement team reached an inappropriate overall conclusion on the subject matter of the engagement, (3) the engagement report is not appropriate in the circumstances, or (4) the firm is not independent of its client.

18. In a review of interim financial information, the firm may grant permission to the client to use the engagement report (or communicate an engagement conclusion to its client, if no report is issued) only after the engagement quality reviewer provides concurring approval of issuance.

Documentation of an Engagement Quality Review

19. Documentation of an engagement quality review should contain sufficient information to enable an experienced auditor, having no previous connection with the engagement, to understand the procedures performed by the engagement quality reviewer, and others who assisted the reviewer, to comply with the provisions of this standard, including information that identifies:

- a. The engagement quality reviewer, and others who assisted the reviewer,
- b. The documents reviewed by the engagement quality reviewer, and others who assisted the reviewer,
- c. The date the engagement quality reviewer provided concurring approval of issuance or, if no concurring approval of issuance was provided, the reasons for not providing the approval.

20. Documentation of an engagement quality review should be included in the engagement documentation.

21. The requirements related to retention of and subsequent changes to audit documentation in PCAOB Auditing Standard No. 3, *Audit Documentation*, apply with respect to the documentation of the engagement quality review.

Conforming Amendment to PCAOB Interim Quality Control Standards

QC sec. 20, "System of Quality Control for a CPA Firm's Accounting and Auditing Practice"

QC section ("sec.") 20, "System of Quality Control for a CPA Firm's Accounting and Auditing Practice" of the Board's interim quality control standards is amended as follows –

The third sentence of paragraph .18 of QC sec. 20 is replaced with the following sentence:

These policies and procedures also should address engagement quality reviews pursuant to PCAOB Auditing Standard No. 7, *Engagement Quality Review*.

II. Board's Statement of the Purpose of, and Statutory Basis for, the Proposed Rules

In its filing with the Commission, the Board included statements concerning the purpose of, and basis for, the proposed rules and discussed any comments it received on the proposed rules. The text of these statements may be examined at the places specified in Item IV below. The Board has prepared summaries, set forth in sections A, B, and C below, of the most significant aspects of such statements.

A. Board's Statement of the Purpose of, and Statutory Basis for, the Proposed Rules

(a) Purpose

Section 103 of the Sarbanes-Oxley Act (the "Act") directs the Board, among other things, to set standards for public company audits, including a requirement for each registered public accounting firm to "provide a concurring or second partner review and approval of [each] audit report (and other related information), and concurring approval in its issuance"

As discussed more fully in Exhibit 3, the Board adopted Auditing Standard No. 7 because it believed that a well-performed engagement quality review ("EQR") can serve as an important safeguard against erroneous or insufficiently supported audit opinions and, accordingly, can contribute to audit quality. The proposed rules are intended to enhance the quality of the EQR by strengthening the existing requirements. Auditing Standard No. 7 provides for a rigorous review that will serve as a meaningful check on the work performed by the engagement team and, the Board believes, should increase the likelihood that a registered public accounting firm will catch any significant engagement deficiencies before it issues its audit report. As a result, the Board recognizes that more work may be necessary under Auditing Standard No. 7 than was performed in some concurring reviews under the existing requirements.

Auditing Standard No. 7 requires the engagement quality reviewer (or the "reviewer") to evaluate the significant judgments made and related conclusions reached by the engagement team in forming the overall conclusion on the engagement and in preparing the engagement report. Auditing Standard No. 7 also requires the engagement quality reviewer to perform certain procedures designed to focus the reviewer on those judgments and conclusions. The procedures required of the reviewer by Auditing Standard No. 7 are different in nature from the procedures required of the engagement team. Unlike the engagement team, a reviewer does not perform substantive procedures or obtain sufficient evidence to support an opinion on the financial statements or internal control over financial reporting. If more audit work is necessary before the

reviewer may provide concurring approval of issuance, the engagement team – not the reviewer – is responsible under PCAOB standards for performing the work. In contrast, the reviewer fulfills his or her responsibility to perform an effective review of the engagement under the EQR standard by holding discussions with the engagement team, reviewing documentation, and determining whether he or she can provide concurring approval of issuance.

The proposed rules also amend the Board's interim quality control standards by replacing the third sentence of paragraph .18 of in QC section 20, "System of Quality Control for a CPA Firm's Accounting and Auditing Practice" with a statement indicating that these policies and procedures also should address engagement quality reviews pursuant to PCAOB Auditing Standard No. 7.

(b) Statutory Basis

The statutory basis for the proposed rules is Title I of the Act.

B. Board's Statement on Burden on Competition

The Board does not believe that the proposed rule changes will result in any burden on competition that is not necessary or appropriate in furtherance of the purposes of the Act. The proposed rule changes would apply equally to all registered public accounting firms.

C. Board's Statement on Comments on the Proposed Rules Received from Members, Participants or Others

The Board released the proposed rules for public comment in PCAOB Release No. 2008-002 (February 26, 2008). The Board received 38 written

comments. The Board considered these comments and made significant changes to the initial proposed rules. As a result, the Board again sought public comment in PCOAB Release No. 2009-001 (March 4, 2009). The Board received 30 written comment letters relating to its reproposal of the proposed rules. A copy of PCAOB Release Nos. 2008-002 and 2009-001 and the comment letters received in response to the PCAOB's request for comment in both releases are available on the PCAOB's web site at www.pcaobus.org.

The Board has carefully considered all comments it has received. In response to the written comments received on both the initial and reproposal of the proposed rules, the Board has clarified and modified certain aspects of the proposed rules, as discussed below.

Overview of Auditing Standard No. 7

Overall, commenters preferred the reproposed standard to the original proposal, though some continued to believe that certain provisions were unclear and suggested certain changes to the standard. After considering commenters' feedback, the Board has made several modifications to the EQR standard to provide additional clarity. This section describes the comments received, the Board's response, and changes made in AS No. 7.^{1/}

^{1/} The Board received some comments related to its standard-setting process in general. The Board continuously endeavors to improve its processes, including its standard-setting process, and is considering these comments as it does so.

Applicability of the EQR Requirement

Paragraph 1 of the repropoed standard required an EQR for audit engagements and reviews of interim financial information ("interim reviews"), but not for other engagements performed according to the standards of the PCAOB. For the most part, commenters believed that this provision was appropriate.^{2/} One commenter, however, suggested including the EQR requirements for interim reviews in AU section ("sec.") 722, *Interim Financial Information*, instead of including them as part of the EQR standard to "make it clear that the scope of the procedures performed remain under the umbrella of the objective of a review of interim financial information (which is much different than the scope and objective of an audit)." Because the requirements for the EQR of interim reviews in AS No. 7 are closely related to and described by reference to the requirements for the EQR of an audit, the Board believes it is more appropriate to locate both sets of requirements in the same standard. Accordingly, the Board is adopting the provisions regarding applicability of the EQR standard as repropoed.

Statement of Objective

The repropoed standard included a statement of objective intended to focus reviewers on the overall purpose of the standard as they carry out the more specific EQR requirements. As repropoed, the objective of the engagement

^{2/} One commenter did not believe that an EQR should be required for interim reviews because of concerns about the scope of the EQR for interim reviews. The section entitled *Specifically Required Procedures in the EQR of an Interim Review* discusses the EQR requirements for interim reviews.

quality reviewer was "to perform an evaluation of the significant judgments made by the engagement team and the conclusions reached in forming the overall conclusion on the engagement and in preparing the engagement report, if a report is to be issued, in order to determine whether to provide concurring approval of issuance."

Most commenters agreed that the EQR standard should include a statement of objective. While some believed the objective was appropriate as repropoed, several suggested substituting the phrase "related conclusions reached" for "the conclusions reached" to indicate that the reviewer is required to evaluate conclusions relating to significant judgments, rather than all conclusions. In addition, some commenters suggested making the objective less vague, while others wanted the Board to broaden it or make it less procedural.

After considering these comments, the Board has, as suggested by commenters, revised the objective so that it refers to "significant judgments made by the engagement team^{3/} and the *related* conclusions reached" (emphasis added). This change should help reviewers maintain their focus on areas of the engagement that are most likely to contain a significant engagement deficiency. With this revision, the Board believes the statement of objective establishes, at the appropriate level of detail, a framework for the performance of the EQR that

^{3/} Because the engagement partner has final responsibility for the engagement, he or she has final responsibility for the significant judgments made during the engagement, notwithstanding any involvement in or responsibility for those judgments by firm personnel outside of the engagement team, such as members of the firm's national office. Accordingly the "significant judgments made by the engagement team" include all of the significant judgments made during the engagement.

is consistent with the specific requirements in AS No. 7. Corresponding changes have been made in paragraphs 9 and 14, which describe the scope of the EQR for audits and interim reviews, respectively. The reviewer achieves his or her objective by complying with the specific requirements of the standard.

Qualifications of the Engagement Quality Reviewer

In order to provide for a high-quality EQR, the repropoed standard described the qualifications that any reviewer would be required to meet. These provisions were designed to provide assurance that the reviewer could effectively perform an EQR of the particular engagement under review. At the same time, the provisions recognized that smaller firms may have few partners – and, in the case of sole practitioners, no additional partners – available in-house to perform the EQR.

Accordingly, the repropoed standard required an engagement quality reviewer from within the firm issuing the engagement report to be a partner or another individual in an equivalent position, but also allowed a qualified individual from outside the firm to perform the EQR. In either event, the repropoed standard required the reviewer to be an associated person^{4/} of a registered public

^{4/} For clarity, in paragraph 3 of AS No. 7, the Board added a reference to Rule1001(p)(i), which defines the term "associated person of a registered public accounting firm." A person not already associated with a registered firm can enter into a relationship with the firm issuing the report such that the person would become associated with that firm by performing the review. Specifically, a person not already associated with a firm would become associated with the firm issuing the report if *he or she* (rather than, or in addition to, his or her firm or other employer): (1) receives compensation from the firm issuing the report for performing the review or (2) performs the review as agent for the firm issuing the report. For example, if the firm issuing the report contracts directly with an employee of an unregistered accounting firm to perform the

accounting firm.^{5/} The repropoed standard also included a general competence requirement and requirements related to the reviewer's independence, integrity, and objectivity.

In-House Reviewer: Partner or an Individual in an Equivalent Position

The requirement in the repropoed standard for a reviewer from within the firm to be a partner or an individual in an equivalent position was intended to address concerns expressed by some commenters on the original proposal about the authority of the engagement quality reviewer relative to that of the engagement partner. Because the EQR is intended to be an objective second look at work performed by the engagement team, the reviewer should be able to withstand pressure from the engagement partner or other firm personnel, such as members of the firm's national office. As described in the repropoing release, the Board believed that concerns about authority will most often arise when the reviewer and the engagement partner work at the same firm. The Board also believed that a standard based on perceptions of relative authority within a firm would not be sufficiently clear to be workable. Accordingly, the Board attempted to address these concerns with a requirement that an in-house reviewer – but not one from outside the firm – be a partner or person in an equivalent position.

engagement quality review, that person would become associated with the firm issuing the report by virtue of that independent contractor relationship.

^{5/} A registered public accounting firm has an obligation to secure and enforce consents to cooperate with the Board from each associated person of the firm, see Section 102(b)(3) of the Act, including those who become associated with the firm by performing the review. The Board also may directly sanction any such person who fails to cooperate in an investigation or inspection. See Section 105(b)(3) of the Act and PCAOB Rules 5110 and 4006.

While some commenters supported the reposed requirement, others disagreed with it, generally because, in their view, being a partner or person in an equivalent position would not necessarily ensure that the reviewer possesses the qualities required to perform the EQR. These commenters noted that partners as well as non-partners may be subject to internal pressure within the firm to provide concurring approval of issuance. In addition, in one commenter's view, it would be burdensome for one-partner firms to hire an outside reviewer to comply with this requirement. Finally, some commenters also asked the Board to define the term "equivalent position."

While both partners and non-partners may experience pressure within the firm to provide concurring approval of issuance, the Board continues to believe that the reposed requirement is the most appropriate way to address this issue. Partnership is not a perfect proxy for authority, but a partner is more likely to possess sufficient authority to conduct the EQR than a non-partner. The Board continues to believe that a requirement based on perceptions of authority would not be workable. Accordingly, the Board is adopting this requirement substantially as reposed.^{6/} At a firm that is not organized as a partnership, "an individual in an equivalent position" is someone with the degree of authority and responsibility of a partner in a firm that is organized as a partnership.

^{6/} One commenter suggested that the phrasing of the reposed standard did not establish a requirement for the in-house reviewer to be a partner because it stated that the reviewer "may be" a partner, a person in an equivalent position, or an individual outside the firm. While the use of "may" in that context imposed a requirement, to avoid any confusion on this point the Board has rephrased the requirement in paragraph 3 of AS No. 7 to use the word "must."

Qualified Reviewer from Outside the Firm

As noted above, the repropose standard also allowed a qualified reviewer from outside the firm to conduct the review. In the repropose release, the Board expressed the view that allowing a sufficiently qualified professor or other individual not employed by an accounting firm to perform the EQR should not negatively affect audit quality and may mitigate the compliance burden on sole practitioners and smaller firms. The Board sought comment on whether a qualified accountant who is not employed by an accounting firm should be allowed to conduct the EQR.^{7/}

The majority of commenters on this topic did not oppose the repropose provision. Some commenters, however, cautioned that reviewers from outside an accounting firm may not necessarily have the required technical expertise or recent audit experience. One commenter believed that allowing the use of such outside reviewers could "hamper the existing independence rules,"^{8/} increase costs, and limit the potential growth of partners.

After considering these comments, the Board continues to believe that the EQR standard can – and should – allow firms the proposed flexibility in choosing a reviewer, provided that reviewer meets the competence and other qualification requirements. According to these requirements, as discussed below, any

^{7/} As noted in the repropose release, under the existing requirement a firm may seek a waiver to engage an outside experienced individual to perform the EQR. Because AS No. 7 allows a firm to use an outside reviewer, such a waiver is not necessary under AS No. 7.

^{8/} The comment did not explain how the independence rules would be hampered.

reviewer would have to have the level of knowledge and competence related to accounting, auditing, and financial reporting required to serve as the person who has overall responsibility for the engagement under review. Accordingly, while some persons from outside a firm might not have the required qualifications, those who do can effectively perform the EQR.^{9/}

The Board also does not agree that allowing the use of a reviewer from outside the firm issuing the report would negatively affect the application or enforcement of the independence rules. As the Board noted in the reproposing release, it will continue to consider anyone who performs the EQR to be an "audit partner" and a member of the "audit engagement team" for purposes of independence requirements.^{10/} In addition, because AS No. 7 would not require a firm to use an outside reviewer, allowing a firm to do so should not increase costs or limit the potential growth of partners. Any firm that is concerned that invoking the flexibility provided by the EQR standard would raise its costs or impede the development of its partners could, simply, decline to do so and use a reviewer from within the firm if one is available.

When considering an outside individual for the role of the engagement quality reviewer, the firm will likely need to make additional inquiries to obtain necessary information about the individual's qualifications. For example, while information about independence of the firm's partners is typically collected and

^{9/} Similarly, a reviewer does not meet all of the qualification requirements in AS No. 7 by virtue of his or her status as a partner or employee of an accounting firm.

^{10/} See Rule 2-01(f) of Regulation S-X, 17 C.F.R. § 210.2-01(f), for the definitions of "audit partner" and "audit engagement team."

evaluated as part of the periodic independence review, information about the independence of an outside reviewer will likely need to be requested and evaluated as part of the reviewer selection process. Firms also likely know more about the competence of their own partners than of an outside reviewer.

General Competence Requirement

As noted above, the reproposed standard, like the original proposal, included a requirement for the reviewer to "possess the level of knowledge and competence related to accounting, auditing, and financial reporting required to serve as the person who has overall responsibility for the same type of engagement." This provision was intended to set a minimum requirement for those who would perform the EQR. In response to comments on the original proposal, the reproposing release explained that this provision, by its terms, did not require the engagement quality reviewer's knowledge and competence to match those of the engagement partner, or for the reviewer to be a "clone" of the engagement partner.^{11/}

Some commenters reiterated their concerns that the engagement quality reviewer's skills would be expected to match those of the engagement partner, and that such a requirement could cause resource constraints for smaller firms.

^{11/} Specifically, the reproposing release noted:

The general competence provision merely sets a minimum requirement for those who would perform the EQR, but it does not require the reviewer's competence to match that of the engagement partner. In many cases, both individuals' competence will exceed the minimum level prescribed, but there is no requirement that they do so in tandem, or even at all.

Other commenters suggested modifying the general competence provision by stating that the reviewer's competence should be established based on the facts and circumstances of the engagement, or describing the required qualifications from the reviewer's perspective, rather than by comparing them to the qualifications of the engagement partner. Finally, some commenters suggested including in the EQR standard a statement that the reviewer may obtain the required level of knowledge and competence through utilizing assistants.

The Board continues to believe that if a minimum level of knowledge and competence in accounting, auditing, and financial reporting is required to conduct an audit, it is similarly necessary to effectively review that audit.^{12/} The reviewer is not required to possess other competencies, e.g., those related to communication or management skills, that the engagement partner may have.

Accordingly, the Board is adopting the general competence provision substantially as proposed. The Board is, however, modifying the requirement to clarify further that the determination of what constitutes the appropriate level of knowledge and competence should be based on the circumstances of the engagement, including the size and complexity of the business under audit or under interim review.^{13/} In AS No. 7, the Board replaced the phrase "the same type of engagement" with "the engagement." The new phrasing focuses the

^{12/} While a reviewer may use assistants in performing the EQR, the reviewer's own skills should meet the requirements of AS No. 7.

^{13/} Footnote 18 on page 9 of the original release stated, "The determination of what constitutes the appropriate level of knowledge and competence should be based on the circumstances of the engagement, including the size or complexity of the business."

reviewer on the particular engagement under review, rather than that "type" of engagement.^{14/} Firms that do not have partners that meet this general competence requirement available to perform the EQR may engage an outside reviewer to perform an EQR.

Independence, Integrity, and Objectivity

Like the original proposal, the repropoed standard required the reviewer to be independent of the company, perform the review with integrity, and maintain objectivity. Comments on the reproposal focused on two provisions regarding objectivity – the prohibition against the reviewer supervising the engagement team and the two-year "cooling-off" period before the engagement partner could perform the EQR.

Supervision of the Engagement Team

The repropoed standard provided that to maintain objectivity the engagement quality reviewer should not, among other things, "supervise the engagement team with respect to the engagement subject to the engagement quality review." The phrase "subject to the engagement quality review" was intended to clarify that partners with leadership responsibilities in a firm, region,

^{14/} In addition, to simplify the text of AS No. 7, the Board replaced the phrase "person with overall responsibility for the engagement" with the term "engagement partner." Footnote 3 of AS No. 7 explains that the term "engagement partner" has the same meaning as the phrases the "auditor with final responsibility for the audit," as described in AU sec. 311, *Planning and Supervision*, and the "practitioner-in-charge of an engagement," as described in PCAOB interim quality control standard QC sec. 40, *The Personnel Management Element of a Firm's System of Quality Control-Competencies Required by a Practitioner-in-Charge of an Attest Engagement*. Because all of these terms refer to the same person, this change does not alter the meaning of the EQR standard.

service, or industry practice are not, solely because of those responsibilities, precluded from reviewing any engagement performed by their subordinates in the firm. Some commenters believed that the phrase "subject to the engagement quality review" was not sufficient to clarify this point.

After considering these comments, the Board has decided that the express prohibition against "supervis[ing] the engagement team with respect to the engagement subject to the engagement quality review" is not necessary to effectuate the Board's intent. The remaining two criteria for maintaining objectivity in paragraph 7 of AS No. 7 – not making decisions on behalf of the engagement team and not assuming any responsibilities of the engagement team – are sufficient to preclude those involved in the engagement from serving as the engagement quality reviewer.^{15/} For example, partners (including the engagement partner and other partners on larger engagements), managers, and others who supervise engagement personnel on the audit under review would not qualify under the remaining criteria because they have assumed responsibilities of the engagement team. At the same time, removing the phrase "supervise the engagement team" from AS No. 7 should further clarify that those

^{15/} AS No. 7 does not prohibit the engagement team from consulting with the reviewer, as long as the reviewer maintains his or her objectivity in accordance with paragraph 7. As noted in the reproposing release, such consultations may contribute to audit quality. In addition, one commenter asked the Board to clarify whether a reviewer may consult with the same personnel who previously consulted with the engagement team. The EQR standard does not prohibit the reviewer from holding discussions with such personnel. The reviewer may not, however, use personnel who previously consulted with the engagement team as assistants in performing the review unless they meet the objectivity and other qualification requirements of AS No. 7. To emphasize the requirement that assistants maintain objectivity, the Board added to paragraph 7 of AS No. 7 the phrase "and others who assist the reviewer."

in leadership positions in the firm who did not make decisions for or assume responsibilities of the engagement team may perform the EQR.

The Two-Year "Cooling-Off" Period

The reproposed standard included a provision prohibiting an engagement partner from serving as the engagement quality reviewer for at least two years following his or her last year as the engagement partner.^{16/} The Board included the "cooling-off" period because it believed that it would be harder for an engagement partner who has had overall responsibility for the audit for at least a year to perform the review with the necessary level of objectivity. While a number of commenters expressed general support for a two-year "cooling-off" period, some believed that it could impose an undue hardship on smaller firms, and suggested a shorter "cooling-off" period.

After considering these comments, the Board continues to believe that a "cooling-off" period will be beneficial to audit quality and that a two-year period appropriately safeguards objectivity without imposing unnecessary hardship on most firms. At the same time, the Board recognizes that compliance with this requirement could be difficult for smaller firms with fewer personnel. In its independence rules, the Securities and Exchange Commission ("SEC") exempted certain smaller firms from the audit partner rotation requirements.

Specifically, Rule 2-01(c)(6)(ii) of Regulation S-X provides an exemption for firms

^{16/} SEC independence rules allow engagement partners and concurring partners to serve for five consecutive years, after which they may not serve in either role for another period of five years. Within a five-year period, SEC independence rules do not impose a "cooling-off" period before the engagement partner can serve as the concurring partner. See Rule 2 - 01(c)(6)(i)(A) of Regulation S-X.

with fewer than five issuer audit clients and fewer than ten partners, provided the Board "conducts a review at least once every three years of each of the audit client engagements that would result in a lack of auditor independence under" the SEC partner rotation requirements. The Board believes that this exemption – including the provision regarding Board inspections – also describes an appropriate exemption from the "cooling-off" requirement in the EQR standard. Accordingly, firms that qualify for the exemption from the SEC partner rotation requirements will also be exempt from the "cooling-off" period under AS No. 7.

EQR Process

The Board's goal in proposing an EQR standard was to strengthen the existing requirements for concurring reviews in order to promote a more meaningful review of the work performed by the engagement team. Accordingly, the original proposal described certain procedures that the reviewer was required to perform that were more specific than those in the existing requirements. In response to comments received on the original proposal, the Board clarified some of the specifically required procedures and included, in a separate section in the repropoed standard, tailored requirements for an EQR of an interim review.

In general, commenters believed that the repropoed standard described the requirements of the EQR more clearly than the original proposal. However, a number of commenters suggested additional modifications that, in their view, would further clarify the Board's intent and ensure consistency of the

requirements with the statement of objective. As described below, after considering these comments, the Board has modified certain of these requirements.

Terminology Used to Describe the Required Procedures

Several commenters noted that the specifically required procedures in paragraphs 9, 10, 14, and 15 of the repropoed standard were described using different, but in some cases similar, terms such as "determine," "evaluate," "identify," "read," and "review," which some commenters found confusing. In one commenter's view, the terms "determine," "identify," and "evaluate" may require the reviewer to perform procedures that are similar in scope to the procedures performed by the engagement partner. The commenters asked the Board to clarify the terminology in these sections of the EQR standard.

While the Board does not believe that this terminology required the reviewer to perform procedures that are appropriately performed by the engagement partner, it does agree that the terminology should not be confusing. Accordingly, the Board reduced the number of terms used in AS No. 7, so that the required procedures in paragraphs 9, 10, 14, and 15 are described using two terms, "evaluate" and "review" – with one exception. Because AU sec. 550, *Other Information in Documents Containing Audited Financial Statements*, requires the auditor to *read* other information in documents containing the financial statements to be filed with the SEC, paragraphs 10.g and 15.e of AS No. 7, like in the original and repropoed standards, also require the reviewer to *read* such

other information and evaluate whether the engagement team has taken appropriate action with respect to any material inconsistencies with the financial statements or interim financial information, respectively, or material misstatements of fact of which the engagement quality reviewer is aware.

Review of Documentation

A number of commenters viewed the statement in paragraphs 9 and 14 of the repropoed standard that "the reviewer should perform the procedures . . . by reviewing documentation" as too open-ended.^{17/} Commenters were concerned that this provision could be interpreted to require the review of all of the engagement documentation.

The Board did not intend to require – and the repropoed provision did not require – the reviewer to review all of the engagement documentation. Nevertheless, to clarify this point, the Board has added the phrase "to the extent necessary to satisfy the requirements" of paragraphs 10 and 11, in an EQR of an audit, and 15 and 16, in an EQR of an interim review. As a practical matter, the reviewer cannot comply with the requirements of the EQR standard without holding discussions with the engagement partner and reviewing documentation. AS No. 7 requires the reviewer to hold sufficient discussions with the engagement partner and other members of the engagement team and review sufficient documentation to perform the required procedures with due

^{17/} That statement was intended, along with other changes in the repropoed standard, to clarify that the EQR is a review of the engagement team's work rather than a second audit. See page 17 of the repropoing release.

professional care. What is sufficient will necessarily depend on the facts and circumstances of the particular engagement under review. Auditors often document their significant judgments and conclusions in various summary documents, which could serve as a starting point for the reviewer's evaluation of the engagement team's work.

Paragraph 11 of the repropoed standard required the reviewer, in an EQR of an audit, to evaluate whether the engagement documentation that he or she reviewed when performing the procedures required by paragraph 10 indicates that the engagement team responded appropriately to significant risks and supports the conclusions reached by the engagement team with respect to the matters reviewed. One commenter suggested adding a requirement to paragraph 11 to evaluate engagement documentation for compliance with the requirements of Auditing Standard No. 3, *Audit Documentation* ("AS No. 3"). The Board originally proposed such a requirement but, in response to comments, did not include it in the repropoed standard.^{18/} The Board continues to believe that the documentation review requirements of paragraph 11 of the repropoed standard are appropriate and is adopting them as repropoed.

In an EQR of an interim review, paragraph 16 of the repropoed standard required the reviewer to evaluate whether the engagement documentation that he or she reviewed "[i]ndicates that the engagement team responded appropriately to significant risks," and "[s]upports the conclusions reached by the

^{18/} Commenters suggested that such a requirement would duplicate the documentation review performed by the engagement partner.

engagement team with respect to the matters reviewed." Some commenters noted that the auditor is not required to identify significant risks in a review of interim financial information and suggested not including a corresponding requirement in the EQR standard. The Board agrees and has not included this requirement in AS No. 7.

Specifically Required Procedures in the EQR of an Audit

Like the original proposal, the repropoed standard required certain procedures designed to give the reviewer the necessary information to evaluate the engagement team's significant judgments and conclusions. In response to comments on the original proposal, the Board made changes to these provisions in the repropoed standard that were intended to clarify that the reviewer performs the EQR by reviewing the engagement team's work, rather than by auditing the company himself or herself. Some commenters suggested that the specifically required procedures in the repropoed standard needed additional clarification.

In the view of several commenters, the repropoed standard did not clearly articulate the requirement for the reviewer to focus on the significant judgments made and the related conclusions reached by the engagement team. These commenters believed that the repropoed standard might be interpreted as requiring the review of all of the engagement team's judgments and conclusions. In response, AS No. 7 refers to "significant judgments" instead of "judgments" in describing certain of the required procedures.

The Board also clarified the wording of paragraph 10.b of the repropoed standard, which required the reviewer to "evaluate the risk assessments and audit responses" Some commenters expressed concern that this formulation required a review of audit responses for all areas of the audit. In response, AS No. 7 more specifically requires the reviewer to evaluate the engagement team's audit responses to significant risks identified by the engagement team and other significant risks identified by the engagement quality reviewer through performance of the procedures required by the EQR standard.^{19/} This change should help focus reviewers on areas of the audit that are more likely to contain a significant engagement deficiency.

Some commenters also expressed concern about the requirements in paragraphs 10.e and 10.f of the repropoed standard to determine whether appropriate matters have been communicated to the audit committee, management, and others; and to determine whether appropriate consultations have taken place on difficult or contentious matters. According to these commenters, a requirement to determine whether all of the communications or consultations have taken place rather than to evaluate the engagement team's communications and consultations was inconsistent with the objective of the

^{19/} The term "significant risk" is defined in the Board's recently proposed auditing standard on identifying and assessing risks of material misstatement to mean a "risk of material misstatement that is important enough to require special audit consideration." PCAOB Release No. 2008-006, *Proposed Auditing Standards Related to the Auditor's Assessment of and Response to Risk and Conforming Amendments to PCAOB Standards* (October 21, 2008). The Board intends that definition to apply to the EQR standard as well. The Board included this definition in a note to paragraph 10.b of AS No. 7. If, at the conclusion of the above mentioned rulemaking, the Board adopts a definition of significant risk that is different from that proposed, the Board will make a conforming change to the EQR standard.

EQR. In response, the Board replaced the phrase "determine if" with "based on the procedures required by this standard, evaluate whether." This change should tailor the specific requirements more closely to the overall objective. The Board also placed these paragraphs after the other required procedures in paragraph 10 to emphasize that the reviewer performs the evaluation required by these paragraphs based on the information obtained through the other procedures required by the EQR standard, and made a corresponding change in paragraph 15 for the EQR of an interim review.

Specifically Required Procedures in the EQR of an Interim Review

In response to comments on the original proposal, the Board included in the repropoed standard separate requirements for reviewing audits and interim reviews. The EQR requirements for interim reviews were based on the requirements for an EQR of an audit but were tailored to the different procedures performed in an interim review. A number of commenters were supportive of including separate requirements for the EQR of interim reviews in the repropoed standard. Some commenters, as discussed below, suggested modifications to those requirements.

Paragraph 15.a of the repropoed standard required the evaluation of engagement planning, including the consideration of the firm's recent engagement experience with the company and risks identified in connection with the firm's client acceptance and retention process; the company's business, recent significant activities, and related financial reporting issues and risks; and

the nature of identified risks of material misstatement due to fraud. In one commenter's view, that paragraph might suggest that an interim review should include the same type of risk assessment as an audit. After considering this comment, the Board disagrees. Paragraph 15.a does not impose a requirement on the engagement team to identify risks as part of an interim review. Rather, it requires the reviewer to evaluate the engagement team's consideration of risks that have already been identified, e.g., during the preceding year's audit.

Additionally, three commenters recommended not requiring the EQR of an interim review to include an evaluation of judgments made about the severity and disposition of identified control deficiencies. In one commenter's view, such an evaluation would be inconsistent with the scope of an interim review. AU sec. 722.07, provides that the auditor:

should perform limited procedures quarterly to provide a basis for determining whether he or she has become aware of any material modifications that, in the auditor's judgment, should be made to the disclosures about changes in internal control over financial reporting in order for the certifications to be accurate and to comply with the requirements of Section 302 of the Act.

In response, the Board modified the requirement in paragraph 15.b in AS No. 7 to be more consistent with the requirements of AU sec. 722. Accordingly, AS No. 7 requires the reviewer, among other things, to evaluate

significant judgments made about any material modifications that should be made to the disclosures about changes in internal control over financial reporting.

Paragraph 15.c of the reposed standard required the reviewer, in the EQR of an interim review, to "[r]ead the interim financial information for all periods presented and for the immediately preceding interim period, management's disclosure for the period under review, if any, about changes in internal control over financial reporting, and the related engagement report, if a report is to be filed with the SEC." Some commenters suggested that the reviewer should be required to read the engagement report even when the issuer is not required to include the report in an SEC filing. The Board agrees and, accordingly, changed "to be filed with the SEC" to "to be issued."^{20/}

Concurring Approval of Issuance

For an EQR of an audit, paragraph 12 of the reposed standard provided that the reviewer "may provide concurring approval of issuance only if, after performing with due professional care the review required by this standard, he or she is not aware of a significant engagement deficiency." A note to the same paragraph describes a "significant engagement deficiency" as any of the

^{20/} Additionally, one commenter recommended not requiring the reviewer to read interim financial information "for the immediately preceding interim period" because it was not clear, to this commenter, what one would review when performing the EQR for the first quarter. AU sec. 722.16 requires the accountant to apply analytical procedures to the interim financial information, which should include, among other things, comparing the quarterly interim financial information with comparable information for the immediately preceding interim period (i.e., the fourth quarter of the prior year, in a first quarter interim review). Because the Board believes the reposed requirement is appropriately within the scope of an EQR for an interim review, it has retained it in AS No. 7.

four conditions described in the original proposal.^{21/} The reposed requirements for providing concurring approval of issuance in an EQR of an interim review were the same, except that the first of these four conditions was modified in light of the differences between an interim review and an audit. Specifically, in an EQR of an interim review, the first condition was "the engagement team failed to perform interim review procedures necessary in the circumstances of the engagement" rather than "the engagement team failed to obtain sufficient appropriate evidence in accordance with the standards of the PCAOB."

Commenters generally believed that the concurring approval of issuance provision was appropriately described, though one recommended excluding the reference to "due professional care" from the EQR standard because AU sec. 230, *Due Professional Care in the Performance of Work*, already imposes an overall requirement on auditors to exercise due professional care. Many commenters, however, were critical of the reposing release's description of the reposed requirement. A significant number of commenters objected to, or stated that they disagreed with, the statement in the reposing release that the requirement to exercise due professional care imposes on the engagement quality reviewer essentially the same requirement as the "knows, or should know based on the requirements of this standard" formulation that was originally

^{21/} As included in the reposed standard, these conditions were: (1) the engagement team failed to obtain sufficient appropriate evidence in accordance with the standards of the PCAOB; (2) the engagement team reached an inappropriate overall conclusion on the subject matter of the engagement; (3) the engagement report is not appropriate in the circumstances; or (4) the firm is not independent of its client.

proposed. Some suggested that the Board is redefining the meaning of due professional care. One commenter stated that "[a] standard of 'knows, or should know' is akin to a strict liability requirement for engagement deficiencies," while another commenter suggested that the Board "clarify that in this context, 'due professional care' is not a negligence standard."

After considering the comments, the Board is adopting the concurring approval of issuance requirement as repropoed. While auditors are already required to exercise due professional care in discharging their responsibilities, comments, as noted above and in the repropoing release, have reflected some confusion about the applicable standard of care in an EQR. Accordingly, reference to due professional care in the requirement is appropriate.

The Board is not redefining due professional care in the context of the EQR standard. As the Board noted in the repropoing release, AU sec. 230 describes due professional care as "reasonable care and diligence" and makes clear that an auditor who acts negligently, i.e., without "reasonable care and diligence," breaches the duty to exercise due professional care.^{22/} Due professional care, as described in AU sec. 230, imposes neither a strict liability nor an actual knowledge standard. The Board intends the term to mean "reasonable care and diligence," as described in AU sec. 230.

The application of a negligence standard to the concurring approval of issuance provision means, as noted in the repropoing release, that "a reviewer

^{22/} See AU sec. 230.03.

cannot evade responsibility because, as a result of an inadequate review, he or she did not discover a problem that a reasonably careful and diligent review would have revealed."^{23/} For that reason, the provision requires the reviewer to perform the required review with due professional care as a prerequisite to providing concurring approval of issuance. A qualified reviewer who has done so will, necessarily, have discovered any significant engagement deficiencies that could reasonably have been discovered under the circumstances. Accordingly, under AS No. 7, such a reviewer may provide concurring approval of issuance if "he or she is not aware of a significant engagement deficiency." Because a reviewer who has not performed the required review with due professional care might not have discovered any significant engagement deficiencies that could reasonably have been discovered under the circumstances – i.e., those the reviewer reasonably should know about – such a reviewer may not, consistent with the standard, provide concurring approval of issuance.

Documentation of the EQR

The reproposed standard required the EQR documentation to contain sufficient information to identify: who performed the review, the documents reviewed, whether and when concurring approval of issuance was provided or

^{23/} Of course, to impose the more severe sanctions authorized under the Act, such as a permanent bar or permanent revocation of registration, the Board must establish "(A) intentional or knowing conduct, including reckless conduct, that results in violation of the applicable statutory, regulatory, or professional standard; or (B) repeated instances of negligent conduct, each resulting in a violation of the applicable statutory, regulatory, or professional standard." Section 105(c)(5) of the Act; see also Rules on Investigations and Adjudications, PCAOB Release No. 2003-015, Appendix 2 at A2-76 (September 29, 2003) (discussing Section 105(c)(5)).

the reasons for not providing the approval, and the significant discussions held, including the details of such discussions. These provisions were intended to respond to comments expressing concern that the originally proposed documentation requirements were overly detailed and would result in duplication of the engagement team's work. Some commenters reiterated their concerns that some of the repropoed requirements were duplicative of requirements to document the engagement itself or overly burdensome.

The Board continues to believe that it is necessary to strengthen the documentation requirements in the interim standard to provide for an informative record of the work performed during the EQR. At the same time, the Board has reconsidered its approach to the documentation requirement in light of the comments received. As described below, the Board has added a general requirement that places the specific requirements in the context of the overall purpose of EQR documentation – to provide a record of how the reviewer carried out the review in accordance with the standard's requirements.

Specifically, paragraph 19 of AS No. 7 includes a requirement for the engagement documentation to contain sufficient information to enable an experienced auditor,^{24/} having no previous connection with the engagement, to understand the procedures performed by the engagement quality reviewer, and others who assisted the reviewer, to comply with the provisions of the

^{24/} As described in paragraph 6 of AS No. 3, "[a]n experienced auditor has a reasonable understanding of audit activities and has studied the company's industry as well as the accounting and auditing issues relevant to the industry."

standard.^{25/} This provision is similar to the audit documentation requirement in paragraph 6 of AS No. 3, and should clarify how the more specific requirements are meant to apply in particular circumstances.

For example, if a reviewer identified a significant engagement deficiency to be addressed by the engagement team, the engagement team should document its response to the identified deficiency in accordance with AS No. 3. Because AS No. 7 does not require duplication of documentation prepared by the engagement team, the engagement quality reviewer does not have to separately document the engagement team's response. Rather, the EQR documentation should contain sufficient information to enable an experienced auditor, having no previous connection with the engagement, to understand, e.g., the significant deficiency identified, how the reviewer communicated the deficiency to the engagement team, why such matter was important, and how the reviewer evaluated the engagement team's response. Similarly, if the reviewer participated in the discussion of the potential for material misstatement due to fraud,^{26/} and the engagement team documented the discussion in accordance with AS No. 3, AS No. 7 only requires the engagement quality reviewer or reviewer's assistants to prepare separate documentation if the documentation prepared by the engagement team does not contain sufficient information to enable an experienced auditor, having no previous connection with the engagement, to

^{25/} Additionally, for clarity of presentation, the Board moved the requirement to include documentation of an EQR in the engagement documentation from paragraph 19 to a new paragraph 20 in AS No. 7.

^{26/} See paragraph .14 of AU sec. 316, *Consideration of Fraud in a Financial Statement Audit*.

understand the procedures performed by the engagement quality reviewer, and others who assisted the reviewer, to comply with the provisions of AS No. 7.

In response to comments, the Board also considered whether modifications were necessary to the specific requirements. First, the Board received several comments related to the provisions of repropose paragraph 19.b, which required the EQR documentation to contain information sufficient to identify the documents reviewed. One commenter believed that a reviewer "may feel compelled to engage in an unnecessary review of additional documents in order to compile a more 'complete' list." Conversely, another commenter believed that the reviewer would be discouraged "to inspect one or more documents than he or she otherwise might or should, thus reducing the quality of the EQR." Some commenters suggested clarifying how the documents should be identified as "reviewed" (i.e., electronically or manually), or suggested limiting the scope of paragraph 19.b to "significant documents."

After considering these comments, the Board has decided to include this requirement in AS No. 7. Identifying a document as reviewed by the engagement quality reviewer should not be unduly burdensome, and will provide an informative record. Such a record could provide registered firms, and the Board, with better information about the EQR, which can be used to evaluate and improve the EQR process. The Board believes it is unnecessary to require in the standard a particular document identification method, such as electronic or manual signature. Rather, this should be determined by each firm individually.

Second, a number of commenters believed that the requirement in paragraph 19.c to document details of significant discussions held by the reviewer, and others who assisted the reviewer, would not improve audit quality and that it would be costly to implement. These commenters suggested that the reviewer might not be able to determine whether a discussion is significant at the time a discussion is held and therefore feel compelled to document every discussion. In order to make clear that documentation of every discussion is neither required nor a prudent use of resources, the Board has not included an explicit requirement to document discussions in AS No. 7. As explained above, however, if documentation of a particular discussion is necessary "to enable an experienced auditor, having no previous connection with the engagement, to understand the procedures performed . . . to comply with the provisions of th[e] standard," such documentation is required under the general documentation requirement.

Effective Date

In reproposing the standard, the Board intended to make a final standard effective for EQRs of interim reviews for fiscal years beginning after December 15, 2009 and for EQRs of audits for fiscal years ending on or after December 15, 2009. Several commenters were concerned that the proposed effective date would not allow for sufficient time to train the auditing firm's personnel and implement the new EQR requirements. These commenters recommended that the effective date of the EQR standard be linked to the beginning of an audit period to provide adequate time for registered firms to prepare for adoption. The

Board agrees with the concerns expressed by the commenters and has decided to make AS No. 7 effective, subject to SEC approval, for both the EQR of audits and the EQR of interim reviews for fiscal years beginning on or after December 15, 2009.

Comparison with other EQR Standards

Three commenters suggested that the Board provide a comparison between the EQR standard and standards of other standard-setters on this subject. One commenter noted that because issuer clients often represent a minor part of a smaller firm's audit client base, the audit methodology of such a firm may be based on other standards as well as PCAOB standards. In response, the Board has described certain significant differences between the Board's EQR standard and the analogous standards of the International Auditing and Assurance Standards Board ("IAASB")^{27/} and the Auditing Standards Board ("ASB") of the AICPA^{28/}.

This comparison is provided for informational purposes only and may not represent the views of the ASB or IAASB regarding the interpretation of their standards. It describes only certain provisions of AS No. 7, and is not a substitute for the EQR standard itself. Compliance with AS No. 7 is required for registered

^{27/} International Standard on Quality Control 1, *Quality Control for Firms that Perform Audits and Reviews of Financial Statements, and Other Assurance and Related Services Engagements*, and International Standard on Auditing 220, *Quality Control for an Audit of Financial Statements*, issued in December 2008.

^{28/} AICPA, Statement on Quality Control Standards No. 7, *A Firm's System of Quality Control* (October 2007).

public accounting firms. Compliance with the analogous ASB and IAASB standards is not sufficient to meet the requirements of AS No. 7.

The Board has developed AS No. 7 to enhance the quality of the engagement quality review ("EQR") process by strengthening the provisions of the Board's interim standard.^{29/} Recently, the ASB and IAASB also updated their standards related to the EQR, and the Board considered information in the standards of the ASB and IAASB when developing its new EQR standard. As described in this section, AS No. 7 includes provisions that are similar in terminology and substance to those in the ASB and IAASB standards, and other provisions added as necessary by the Board. For example, the Board included certain provisions in AS No. 7 that are not included in the standards of the ASB or IAASB to: comply with the requirements of the Act; respond to the feedback received on the interim standard from the Board's Standing Advisory Group ("SAG") and information obtained through PCAOB oversight of registered firms; and to ensure consistency of the provisions of AS No. 7 with the provisions and terminology of other relevant standards of the PCAOB.

Some of the provisions of the IAASB standards described in this section are included in the "Application and Other Explanatory Material" section of these standards. That section "does not in itself impose a requirement," but "is relevant

^{29/} The Securities and Exchange Commission Practice Section ("SECPS") of the AICPA Requirements of Membership Sections 1000.08(f); 1000.39, Appendix E.

to the proper application of the requirements of an ISA.^{30/} In contrast, the comparable provisions of AS No. 7 are included in the standard, and establish requirements.

Applicability

PCAOB

Section 103 of the Act requires the Board to adopt an EQR standard for audit engagements.^{31/} Because of the importance of interim financial information to investors, the Board has decided to include a requirement to perform an EQR for reviews of interim financial information performed in accordance with AU section ("sec.") 722, *Interim Financial Information*, ("interim reviews") in the EQR standard. Accordingly, AS No. 7 requires an EQR and concurring approval of issuance for each audit engagement and for each interim review engagement conducted pursuant to the standards of the PCAOB.^{32/}

ASB

SQCS No. 7 does not require an EQR for any type of engagement. Accounting firms should determine whether an EQR is required for any engagement.^{33/}

^{30/} See paragraph A59 of ISA 200, *Overall Objectives of the Independent Auditor and the Conduct of an Audit in Accordance with International Standards on Auditing*.

^{31/} See Section 103(a)(2)(A)(ii) of the Act.

^{32/} See paragraph 1 of AS No. 7.

^{33/} See paragraphs 80-81 and 83 of SQCS No. 7.

IAASB

ISQC 1 requires an EQR only for audits of financial statements of listed entities. Accounting firms should determine whether an EQR is required for any other engagements.^{34/}

Qualifications of a Reviewer*PCAOB*

Associated Person – In order to obtain cooperation with the Board of the individuals that perform an EQR,^{35/} the Board included in AS No. 7 a requirement, according to which the engagement quality reviewer must be an associated person of a registered public accounting firm.^{36/}

A Reviewer from Outside the Firm – Similar to the standards of the ASB and IAASB, AS No. 7 allows a qualified individual from outside the firm to perform an EQR.^{37/}

^{34/} See paragraphs 35(a)-(b) of ISQC 1.

^{35/} A registered public accounting firm has an obligation to secure and enforce consents to cooperate with the Board from each associated person of the firm, see Section 102(b)(3) of the Act, including those who become associated with the firm by performing the review. The Board also may directly sanction any such person who fails to cooperate in an investigation or inspection. See Section 105(b)(3) of the Act and PCAOB Rules 5110 and 4006.

^{36/} See paragraph 3 of AS No. 7.

^{37/} See id.

Partner or Person in an Equivalent Position – Because the EQR is intended to be an objective "second look" at work performed by the engagement team, the reviewer should possess sufficient authority to be able to withstand pressure from the engagement partner or other firm personnel, such as members of the firm's national office. The Board believes that concerns about authority will most often arise when the reviewer and the engagement partner are from the same firm. Therefore, the Board included in AS No. 7 the requirement that an in-house reviewer – but not one from outside the firm – be a partner or another individual in an equivalent position.^{38/}

General Competence Requirement – The Board included in AS No. 7 a requirement for the reviewer to possess the level of knowledge and competence related to accounting, auditing, and financial reporting required to serve as the engagement partner on the engagement under review.^{39/} Without such knowledge and competence, the reviewer would not be able to appropriately evaluate the significant judgments made and related conclusions reached by the engagement team in an audit or an interim review.

^{38/} See *id.*.

^{39/} See paragraph 5 of AS No. 7. PCAOB interim quality control standards describe the competencies required of a person who has the overall responsibility for an engagement (or any practitioner-in-charge of an attest engagement). See QC sec. 40, *The Personnel Management Element of a Firm's System of Quality Control-Competencies Required by a Practitioner-in-Charge of an Attest Engagement*.

Independence, Integrity, and Objectivity – The reviewer must comply with all applicable independence requirements,^{40/} and perform the review with integrity and objectivity.^{41/} The engagement quality reviewer should be able to take a step back and conduct the review from the perspective of an outsider looking in.

Accordingly, AS No. 7 requires that the firm's quality control policies and procedures should include provisions to provide the firm with reasonable assurance that the engagement quality reviewer has sufficient competence, independence, integrity, and objectivity to perform the engagement quality review in accordance with the standards of the PCAOB.^{42/} As described later, the ASB and IAASB contain similar provisions, except the standards of IAASB do not include the direction on independence for the reviewer.

While AS No. 7 does not contain the direction included in the standards of ASB and IAASB that the firm's policies and procedures should establish the degree to which a reviewer can be consulted on the engagement without compromising his or her objectivity,^{43/} or provide for the replacement of the reviewer when the reviewer's ability to perform an objective review has been, or

^{40/} See, e.g., Rule 2-01(c)(6) of Regulation S-X, 17 C.F.R. § 210.2-01(c)(6) (subjecting the engagement quality reviewer to the five-year partner rotation requirement).

^{41/} See ET sec. 102, *Integrity and Objectivity*, and ET sec. 191, *Ethics Rulings on Independence, Integrity, and Objectivity*.

^{42/} See paragraph 4 of AS No. 7.

^{43/} See paragraph 96 of SQCS No.7; paragraph 39(b) of ISQC 1.

may be, impaired,^{44/} such direction is implicit in the requirement of AS No. 7 that a reviewer must maintain objectivity in performing the EQR.^{45/} Importantly, AS No. 7 provides direction on maintaining objectivity, according to which the engagement quality reviewer and others who assist the reviewer should not make decisions on behalf of the engagement team or assume any of the responsibilities of the engagement team.^{46/}

"Cooling-off" period – An engagement quality reviewer is expected to take a fresh, objective look at the engagement. The Board believes that it would be harder for an engagement partner, who has had overall responsibility for the audit for a year or more, to perform the EQR with the necessary level of objectivity. Accordingly, AS No. 7 includes a requirement, according to which the reviewer may not be the person who served as the engagement partner during either of the two audits preceding the audit subject to the EQR. (Registered firms that qualify for the exemption under Rule 2-01(c)(6)(ii) of Regulation S-X, 17 C.F.R. § 210.2-01(c)(6)(ii), are exempt from this requirement.)^{47/}

ASB

SQCS No. 7 requires an auditing firm to establish the engagement quality reviewer qualifications, including those related to experience, authority, and

^{44/} See paragraph 97 of SQCS No. 7; paragraph 41 of ISQC 1.

^{45/} See paragraph 6 of AS No. 7.

^{46/} See paragraph 7 of AS No. 7.

^{47/} See paragraph 8 of AS No. 7.

objectivity.^{48/} SQCS No. 7 describes the engagement quality reviewer as a partner, other person in the firm, qualified external person, or a team made up of such individuals, none of whom is part of the engagement team, with sufficient and appropriate experience and authority to perform the EQR.^{49/} According to SQCS No. 7, what constitutes sufficient and appropriate technical experience, and authority depends on the circumstances of the engagement.^{50/}

SQCS No. 7 does not include a "cooling-off" period, or a requirement for the reviewer to be an associated person of a registered public accounting firm.

Similar to AS No. 7, SQCS No. 7 requires that the firm establish policies and procedures designed to maintain the objectivity of the reviewer, and that such policies and procedures provide that the reviewer should satisfy the independence requirements relating to the engagements reviewed.^{51/} Unlike AS No. 7, SQCS No. 7 does not provide a specific direction on maintaining objectivity. Instead, SQCS No. 7 provides examples of policies and procedures for maintaining the objectivity of the reviewer.^{52/}

IAASB

ISQC 1 requires an auditing firm to establish the engagement quality reviewer qualification requirements, including those related to experience,

^{48/} See paragraphs 92-94 of SQCS No. 7.

^{49/} See paragraph 5.e of SQCS No. 7.

^{50/} See paragraph 93 of SQCS No. 7.

^{51/} See paragraph 94 of SQCS No. 7.

^{52/} See paragraph 95 of SQCS No. 7.

authority, and objectivity.^{53/} The engagement quality reviewer is described as a partner, other person in the firm, suitably qualified external person, or a team made up of such individuals, none of whom is part of the engagement team, with sufficient and appropriate experience and authority to objectively evaluate the significant judgments the engagement team made and the conclusions it reached in formulating the report.^{54/} The application materials in ISQC 1 state that what constitutes sufficient and appropriate technical expertise, experience and authority depends on the circumstances of the engagement.^{55/}

ISQC 1 and ISA 220 do not include reviewer independence or "cooling-off" requirements, or a requirement for the reviewer to be an associated person of a registered public accounting firm.

Similar to AS No. 7, ISQC 1 requires that the firm establish policies and procedures designed to maintain the objectivity of the reviewer.^{56/} Unlike AS No. 7, the IAASB standards do not provide specific direction on maintaining objectivity. Instead, the application materials of ISQC 1 discuss policies and procedures for maintaining the objectivity of the reviewer.^{57/}

^{53/} See paragraphs 39 and 40 of ISQC 1.

^{54/} See paragraph 12(e) of ISQC 1; paragraph 7(c) of ISA 220.

^{55/} See paragraph A47 of the Application and Other Explanatory Materials of ISQC 1.

^{56/} See paragraph 40 of ISQC 1.

^{57/} See paragraph A49 of the Application and Other Explanatory Materials of ISQC 1.

Engagement Quality Review for an Audit

Engagement Quality Review Process

PCAOB

Similar to the standards of the ASB and IAASB, AS No. 7 requires the reviewer to evaluate the significant judgments made and the related conclusions reached by the engagement team in forming the overall conclusion on the engagement and in preparing the engagement report; and to carry out the review through discussions with those performing the engagement and the review of documentation.^{58/}

Further, AS No. 7 specifically requires the reviewer, among other things, to evaluate:

- The significant judgments that relate to engagement planning;^{59/}
- The engagement team's assessment of and audit responses to significant risks, including fraud risks;^{60/} and
- The significant judgments made about identified misstatements and control deficiencies.^{61/}

^{58/} See paragraph 9 of AS No. 7.

^{59/} See paragraph 10.a of AS No. 7.

^{60/} See paragraph 10.b of AS No. 7.

^{61/} See paragraph 10.c of AS No. 7.

Also, AS No. 7 contains a requirement, similar to a requirement for audits of listed entities in ISA 220, according to which the reviewer, based on the procedures required by the standard, should evaluate whether appropriate consultations have taken place on difficult or contentious matters, and review the documentation, including conclusions, of such consultations.^{62/}

According to PCAOB Rule 3520, *Auditor Independence*, "[a] registered public accounting firm and its associated persons must be independent of the firm's audit client throughout the audit and professional engagement period." Because of the importance of compliance with PCAOB and SEC independence requirements, AS No. 7 requires the reviewer to review the engagement team's evaluation of the firm's independence in relation to the engagement.^{63/}

In 2004, the Board adopted Auditing Standard No. 3, *Audit Documentation* ("AS No. 3"). According to paragraph 13 of AS No. 3, the auditor must identify all significant findings or issues in an engagement completion document. AS No. 7 requires the reviewer to review the engagement completion document and confirm with the person who has overall responsibility for the engagement that there are no significant unresolved matters.^{64/}

^{62/} See paragraph 10.h of AS No. 7.

^{63/} See paragraph 10.d of AS No. 7.

^{64/} See paragraph 10.e of AS No. 7.

Similar to the standards of the ASB and IAASB, AS No. 7 requires the reviewer to review the financial statements and the related engagement report.^{65/} Additionally, because an integrated audit includes an audit of internal control over financial reporting,^{66/} AS No. 7 requires the reviewer to review management's report on internal control.^{67/}

An issuer may publish various documents that contain information in addition to audited financial statements and the auditor's report thereon. The auditor is required to read the other information and consider whether such information, or the manner of its presentation, is materially inconsistent with information, or the manner of its presentation, appearing in the financial statements.^{68/} Accordingly, AS No. 7 requires the reviewer to read other information in documents containing the financial statements to be filed with the SEC and evaluate whether the engagement team has taken appropriate action with respect to any material inconsistencies with the financial statements or material misstatements of fact of which the engagement quality reviewer is aware.^{69/}

^{65/} See paragraph 10.f of AS No. 7.

^{66/} PCAOB Auditing Standard No. 5, *An Audit of Internal Control Over Financial Reporting That Is Integrated with An Audit of Financial Statements* establishes requirements and provides direction that apply when an auditor is engaged to perform an audit of management's assessment of the effectiveness of internal control over financial reporting.

^{67/} See paragraph 10.f of AS No. 7.

^{68/} See AU sec. 550, *Other Information in Documents Containing Audited Financial Statements*.

^{69/} See paragraph 10.g of AS No. 7.

Finally, because of the importance to the audit process of effective communication between the auditor and those charged with governance, AS No. 7 requires the reviewer, based on the procedures required by the standard, to evaluate whether appropriate matters have been communicated, or identified for communication, to the audit committee, management, and other parties, such as regulatory bodies.^{70/}

ASB

Similar to AS No. 7, SQCS No. 7 requires that the EQR procedures include an objective evaluation of the significant judgments made by the engagement team and the conclusions reached in formulating the report.^{71/} The EQR performed in accordance with SQCS No. 7 should include: reading the financial statements or other subject matter information and the report and considering whether the report is appropriate; review of selected documentation; and a discussion with the engagement partner regarding significant findings and issues.^{72/}

In addition to the required procedures summarized in the preceding paragraph, an EQR performed in accordance with SQCS No. 7 may include consideration of certain other matters, examples of which are provided in the

^{70/} See paragraph 10.i of AS No. 7.

^{71/} See paragraph 85 of SQCS No. 7.

^{72/} See paragraphs 86 and 87 of SQCS No. 7.

standard. SQCS No. 7 also provides examples of significant judgments that could be made by the engagement team.^{73/}

IAASB

The EQR procedures required by the standards of the IAASB are similar to those required by the ASB.^{74/} Additionally, for audits of listed entities, the IAASB standards require the reviewer to consider: the engagement team's evaluation of the firm's independence in relation to the engagement; and whether appropriate consultation has taken place on matters involving differences of opinion or other difficult or contentious matters, and the conclusions arising from those consultations.^{75/}

Evaluation of Engagement Documentation

PCAOB

AS No. 7 includes a documentation review requirement that is similar to the requirement for audits of listed entities in the IAASB standards. According to AS No. 7, the reviewer should evaluate whether the engagement documentation that he or she reviewed when performing the required EQR procedures indicates that the engagement team responded appropriately to significant risks and

^{73/} See paragraphs 88 and 89 of SQCS No. 7.

^{74/} See paragraph 37 of ISQC 1; paragraph 20 of ISA 220.

^{75/} See paragraphs 38(a) and 38(b) of ISQC 1; paragraphs 21(a) and 21(b) of ISA 220.

supports the conclusions reached by the engagement team with respect to the matters reviewed.^{76/}

ASB

Unlike AS No. 7, SQCS No. 7 does not require the reviewer to evaluate whether the engagement documentation satisfies certain criteria. Instead, SQCS No. 7 states that an EQR may include consideration of whether working papers selected for review reflect the work performed in relation to the significant judgments and support the conclusions reached.^{77/}

IAASB

Similar to AS No. 7, the IAASB standards require, for audits of financial statements of listed entities, that the reviewer consider whether audit documentation selected for review reflects the work performed in relation to the significant judgments and supports the conclusions reached.^{78/}

Concurring Approval of Issuance and Resolution of Differences of Opinion

PCAOB

Under the Act,^{79/} the Board's standard on EQR must require concurring approval of issuance of each audit report. AS No. 7 states that the engagement

^{76/} See paragraph 11 of AS No. 7.

^{77/} See paragraph 88 of SQCS No. 7.

^{78/} See paragraph 38(c) of ISQC 1; paragraph 21(c) of ISA 220.

^{79/} See Section 103(a)(2)(A)(ii) of the Act.

quality reviewer may provide concurring approval of issuance only if, after performing with due professional care the review required by the standard, he or she is not aware of a significant engagement deficiency.^{80/} The firm may grant permission to the client to use the engagement report only after the engagement quality reviewer provides concurring approval of issuance.^{81/}

Unlike the standards of the ASB and IAASB, AS No. 7 does not include an explicit provision for addressing differences of opinion. Firms may develop their own procedures for resolving such differences. Ultimately, however, under the standard, the reviewer may not provide concurring approval of issuance if there remains a significant engagement deficiency. If no concurring approval is provided, AS No. 7 requires that the EQR documentation include information that identifies the reasons for not providing the approval.

ASB

SQCS No. 7 does not include a requirement for the engagement quality reviewer to provide concurring approval of issuance. Instead, SQCS No. 7 requires the EQR be completed before the engagement report is released.^{82/} According to SQCS No. 7, when the engagement quality reviewer makes

^{80/} According to paragraph 12 of AS No. 7, "A *significant engagement deficiency* in an audit exists when (1) the engagement team failed to obtain sufficient appropriate evidence in accordance with the standards of the PCAOB, (2) the engagement team reached an inappropriate overall conclusion on the subject matter of the engagement, (3) the engagement report is not appropriate in the circumstances, or (4) the firm is not independent of its client."

^{81/} See paragraph 13 of AS No. 7.

^{82/} See paragraph 81 of SQCS No. 7.

recommendations that the engagement partner does not accept and the matter is not resolved to the reviewer's satisfaction, the firm's procedures for dealing with differences of opinion apply.^{83/} The firm's policies and procedures should require that conclusions reached be documented and implemented, and the engagement report not be released until the matter, on which the difference of opinion has arisen, is resolved.^{84/}

IAASB

The standards of the IAASB do not include a requirement for the engagement quality reviewer to provide concurring approval of issuance. Instead, the IAASB standards require that the engagement partner should not date the auditor's report until the completion of the EQR.^{85/} If differences of opinion arise between the engagement partner and the engagement quality reviewer, ISA 220 requires the engagement team to follow the firm's policies and procedures for dealing with and resolving differences of opinion.^{86/} ISQC 1 requires the firm to establish policies and procedures for dealing with and resolving differences of opinion between the engagement partner and the engagement quality reviewer. Such policies and procedures shall require that conclusions reached be

^{83/} See paragraph 91 of SQCS No. 7.

^{84/} See paragraph 78 of SQCS No. 7.

^{85/} See paragraph 36 of ISQC 1; paragraph 19(c) of ISA 220.

^{86/} See paragraph 22 of ISA 220.

documented and implemented, and the report not be dated until the matter is resolved.^{87/}

Documentation of an EQR

PCAOB

Because of deficiencies in the documentation of concurring reviews, the Board decided to strengthen the existing documentation requirements. AS No. 7 requires that documentation of an EQR should contain sufficient information to enable an experienced auditor, having no previous connection with the engagement, to understand the procedures performed by the engagement quality reviewer, and others who assisted the reviewer, to comply with the provisions of the standard, including information that identifies: the engagement quality reviewer, and others who assisted the reviewer; the documents reviewed by the engagement quality reviewer and others who assisted the reviewer; and the date the engagement quality reviewer provided concurring approval of issuance or, if no concurring approval of issuance was provided, the reasons for not providing the approval.^{88/}

Unlike the standards of the ASB or the IAASB, AS No. 7 requires that the documentation of an EQR be included in the engagement documentation and

^{87/} See paragraphs 43-44 of ISQC 1.

^{88/} See paragraph 19 of AS No. 7.

provides requirements related to retention of and subsequent changes to the EQR documentation.^{89/}

ASB

According to SQCS No. 7, the documentation of an EQR should state that the procedures required by the firm's policies on EQR have been performed, the EQR has been completed before the report is released, and 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.^{90/}

SQCS No. 7 requires that the firm should: establish procedures designed to maintain the confidentiality, safe custody, integrity, accessibility, and retrievability of engagement documentation; and establish policies and procedures for the retention of engagement documentation for a period sufficient to meet the needs of the firm, professional standards, laws, and regulations.^{91/}

IAASB

The engagement quality reviewer is required to document that the procedures required by the firm's policies on the EQR have been performed, the EQR has been completed on or before the date of the auditor's report, and the reviewer is not aware of any unresolved matters that would cause the reviewer to

^{89/} See paragraphs 20-21 of AS No. 7.

^{90/} See paragraph 99 of SQCS No. 7.

^{91/} See paragraphs 63-71 of SQCS No. 7.

believe that the significant judgments the engagement team made and the conclusions they reached were not appropriate.^{92/}

ISQC 1 requires that the firm should establish policies and procedures related to the completion of the assembly of final engagement files; confidentiality, safe custody, integrity, accessibility and retrievability of engagement documentation; and retention of engagement documentation.^{93/}

III. Date of Effectiveness of the Proposed Rules and Timing for Commission Action

Within 35 days of the date of publication of this notice in the Federal Register or within such longer period (i) as the Commission may designate up to 90 days of such date if it finds such longer period to be appropriate and publishes its reasons for so finding or (ii) as to which the Board consents, the Commission will:

- (a) by order approve such proposed rules; or
- (b) institute proceedings to determine whether the proposed rules should be disapproved.

IV. Solicitation of Comments

Interested persons are invited to submit written data, views and arguments concerning the foregoing, including whether the proposed rules are consistent with the requirements of Title I of the Act. Persons making written submissions should file six copies thereof with the Secretary, Securities and Exchange

^{92/} See paragraph 42 of ISQC 1; paragraph 25 of ISA 220.

^{93/} See paragraphs 45-47 of ISQC 1.

Commission, 100 F Street, NE, Washington, DC 20549. Copies of the submission, all subsequent amendments, all written statements with respect to the proposed rules that are filed with the Commission, and all written communications relating to the proposed rules between the Commission and any person, other than those that may be withheld from the public in accordance with the provisions of 5 U.S.C. 552, will be available for inspection and copying in the Commission's Public Reference Room. Copies of such filing will also be available for inspection and copying at the principal office of the PCAOB. All submissions should refer to File No. PCAOB-2009-02 and should be submitted within [] days.

By the Commission.

Secretary



1666 K Street, NW
 Washington, D.C. 20006
 Telephone: (202) 207-9100
 Facsimile: (202)862-8430
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PROPOSED AUDITING STANDARD –)	
)	PCAOB Release No. 2008-002
ENGAGEMENT QUALITY REVIEW)	February 26, 2008
)	
AND CONFORMING AMENDMENT TO THE)	PCAOB Rulemaking
BOARD'S INTERIM QUALITY CONTROL)	Docket Matter No. 025
STANDARDS)	
)	
)	
)	

Summary: The Public Company Accounting Oversight Board (the "Board" or "PCAOB") is proposing an auditing standard, *Engagement Quality Review*, that would supersede the Board's interim concurring partner review requirement, and a conforming amendment to the Board's interim quality control standards.

Public
 Comment: Interested persons may submit written comments to the Board. Such comments should be sent to the Office of the Secretary, PCAOB, 1666 K Street, N.W., Washington, D.C. 20006-2803. Comments also may be submitted by e-mail to comments@pcaobus.org or through the Board's Web site at www.pcaobus.org. All comments should refer to PCAOB Rulemaking Docket Matter No. 025 in the subject or reference line and should be received by the Board no later than 5:00 PM (EST) on May 12, 2008.

Board
 Contacts: Gregory Scates, Deputy Chief Auditor (202/207-9114; scatesg@pcaobus.org) and Keesha Campbell, Assistant Chief Auditor (202/207-9207); campbellk@pcaobus.org

I. Introduction

Section 103 of the Sarbanes-Oxley Act of 2002 ("the Act") directs the PCAOB to include, in the auditing standards that it adopts, requirements that each registered public accounting firm:



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provide a concurring or second partner review and approval of [each] audit report (and other related information), and concurring approval in its issuance, by a qualified person (as prescribed by the Board) associated with the public accounting firm, other than the person in charge of the audit, or by an independent reviewer (as prescribed by the Board).^{1/}

This mandate placed renewed emphasis on the importance to audit quality of an objective "second look" at the engagement before the firm issues its report. In the Board's view, well-performed engagement quality reviews are an important element in establishing a basis for investor reliance on audits. While some audits also may be subject to *post hoc* internal quality reviews by a firm or a PCAOB inspection, neither procedure is a substitute for a well-performed engagement quality review. An engagement quality review is conducted contemporaneously with the engagement and, thus, may correct a problem before the engagement is completed. Furthermore, under the proposed standard, an engagement quality review would be required on every engagement conducted pursuant to the standards of the PCAOB.

Accordingly, the Board examined its existing requirement with a view toward enhancing the quality of this concurring partner review process. Based on this examination, the PCAOB today is proposing an auditing standard, *Engagement Quality Review*, that would supersede the Board's interim concurring partner review requirement, and a conforming amendment to the Board's interim quality control standards.

A. Background

At the time the PCAOB was established, members of the SEC Practice Section ("SECPS")^{2/} of the American Institute of Certified Public Accountants ("AICPA") had a

^{1/} Section 103(a)(2)(A)(ii) of the Act.

^{2/} The SECPS was formed in 1977 as a voluntary membership organization within the AICPA with the objective of improving the quality of practice by CPA firms before the U.S. Securities and Exchange Commission ("SEC" or "Commission"). On January 8, 1990, the AICPA membership adopted a bylaw amendment to require membership in the SECPS by firms that audit "SEC client[s]," as that term was defined in Appendix D, *Revised Definition of an SEC Client*, of the SECPS Reference Manual (SECPS §1000.38). Firms domiciled outside the United States generally were not members of the SECPS.



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requirement to obtain concurring partner reviews of audit reports on the financial statements of SEC registrants.^{3/} The Board adopted, on April 16, 2003, as part of its interim quality control standards, the SECPS requirement for concurring reviews.^{4/} Currently, that requirement applies only to registered firms that were members of the SECPS as of that date.

Under the Board's existing requirement, the objective of the concurring partner review is to review those significant auditing, accounting, and financial reporting matters that come to the reviewer's attention and the resolution of those matters prior to the issuance of the firm's audit report on the financial statements. The existing requirement, among other things, requires the concurring partner reviewer to: (1) discuss significant accounting, auditing and financial reporting matters with the engagement partner; (2) discuss the engagement team's identification and audit of high-risk transactions and account balances; (3) review documentation of the resolution of significant accounting, auditing, and financial reporting matters, including consultation with firm personnel or others outside of the firm; (4) review the summary of unadjusted audit differences; (5) read the financial statements and the auditor's report; and (6) confirm with the engagement partner that there are no significant unresolved matters.

The interim requirement further provides that, "[o]n the basis of th[e] review, the concurring partner reviewer should conclude that no matters that have come to his or her attention would cause the concurring partner reviewer to believe that" the audit was not performed in accordance with the standards of the PCAOB or that the financial statements are not in conformity with generally accepted accounting principles. Under the interim requirement, the concurring partner review should be completed before the audit report is released.

As part of the Board's process of evaluating the interim concurring partner review requirement, the Board sought the advice of its Standing Advisory Group ("SAG") on

^{3/} See SECPS Requirements of Membership, Section 1000.08(f), *Concurring Partner Review of the Audit Report and the Financial Statements of Commission Registrants*, available at http://www.pcaobus.org/Standards/Interim_Standards/Quality_Control_Standards/SEC_PS_1000.08.aspx#f.

^{4/} See PCAOB Rule 3400T, *Interim Quality Control Standards*.



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two separate occasions.^{5/} The discussions (1) suggested ways in which the Board could develop a new standard that would improve the existing interim requirement and (2) considered how smaller registered public accounting firms could provide for or otherwise obtain cost-effective engagement quality reviews. Some SAG members were of the view that the interim requirement did not provide for a thorough review to achieve the objectives of the requirement and that the reviews generally need to be more robust to provide investors with assurance on the quality of audit engagements. Overall, members were supportive of the Board developing a new standard and suggested that the Board establish requirements to govern the engagement quality reviewer's approval of issuance of the audit report. Some members indicated that the review should be performed in a timely manner and that a new standard should provide some guidance on the reviewer's responsibility to assess the sufficiency of the engagement team's documentation.

In addition to input received at these SAG meetings, the Board considered information on this topic from PCAOB inspections when formulating the proposed standard. The significance and the frequency of non-compliance with the Board's standards that PCAOB inspection teams have identified raise questions regarding the effectiveness of the reviews performed pursuant to the Board's existing concurring partner review requirement. Also, documentation of engagement quality reviews was, in some cases, poor, which suggested a need to enhance the existing standard's documentation requirements.

The Board also considered the findings from recent PCAOB enforcement cases. For example, in one matter the Board found that despite assessing an engagement as presenting "greater than normal risk," the firm, among other things, failed to staff the engagement in accordance with PCAOB standards and did not obtain sufficient competent evidential matter to afford a reasonable basis for its opinion on the financial statements.^{6/} Although the Board's order in that case does not reflect any determination about whether the concurring partner review of the engagement violated PCAOB

^{5/} The Standing Advisory Group discussed this topic at meetings held on June 22, 2004, and October 5, 2005. See webcasts at http://www.pcaobus.org/News_and_Events/Webcasts.aspx#20 and http://www.pcaobus.org/News_and_Events/Webcasts.aspx#32, respectively.

^{6/} See In the Matter of Deloitte & Touche LLP, PCAOB Release No. 105-2007-005 (December 10, 2007).



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standards, it does note that the concurring partner review "was not sufficient under the circumstances to provide the firm with reasonable assurance that its personnel complied with PCAOB standards."^{7/}

Furthermore, the Board considered information on this topic from other sources, including the standards in this area published by the International Auditing and Assurance Standards Board ("IAASB") of the International Federation of Accountants^{8/} and the Auditing Standards Board of the AICPA.^{9/}

^{7/} Id.; see also In the Matter of Williams & Webster, P.S., Kevin J. Williams, CPA, and John G. Webster, CPA, PCAOB Release No. 105-2007-001 (June 12, 2007) (finding that the concurring partner failed to exercise due professional care and objectivity in performing his review and concurred with the decision to issue the audit report even though significant issues he identified remained inadequately addressed).

^{8/} Proposed Redrafted International Standard on Auditing ("ISA") 220, *Quality Control for an Audit of Financial Statements*, requires an engagement quality control review, which is defined as "a process designed to provide an objective evaluation . . . of the significant judgments the engagement team made and the conclusions they reached in formulating the auditor's report." The review should include discussions with the engagement partner, a review of the financial statements and the auditor's report, and consideration of whether the auditor's report is appropriate. It also should include a review of selected working papers relating to the significant judgments the engagement team made and the conclusions they reached.

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*, requires that firms establish policies and procedures for an engagement quality control review that set out the nature, timing, and extent of the review; the criteria for the eligibility of the engagement quality control reviewer; the documentation requirements of the engagement quality control review; and the resolution of differences of opinions.

^{9/} Statement on Quality Control Standards No. 7, *A Firm's System of Quality Control*, contains requirements similar to those in Proposed Redrafted "ISA 220" and Proposed Redrafted "ISQC 1".



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B. Proposed Auditing Standard, *Engagement Quality Review*

The proposed standard would apply to all engagements performed in accordance with the standards of the PCAOB. In addition to requiring certain specified procedures, the proposed standard requires the engagement quality reviewer to assess whether there are areas within the engagement that pose a higher risk that the engagement team failed (1) to obtain sufficient competent evidence or (2) to reach an appropriate conclusion. In such areas, the engagement quality reviewer should 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 conclusions.

Furthermore, the proposed standard includes a new requirement that the engagement quality reviewer must satisfy before providing concurring approval of issuance. As stated above, under the existing requirement, the reviewer has to conclude that no matters have come to his or her attention that would cause the reviewer to believe that the financial statements are not in conformity with generally accepted accounting principles or that the audit was not conducted in accordance with the standards of the PCAOB. Under the proposed standard, the reviewer must not provide concurring approval of issuance if he or she knows, or should know based upon the requirements of the standard, that the engagement team failed to obtain sufficient competent evidence, the engagement team's overall conclusion or report is inappropriate, or the firm is not independent of its client. Concurring approval of issuance would be required before the firm could grant the client permission to use the engagement report (or communicate a conclusion to a client if no report is issued).

In considering how to improve its existing requirement, while the effectiveness of the standard was the guiding principle, the Board also endeavored to draft a standard that would avoid imposing any unnecessary costs. For example, the approach centers the engagement quality reviewer's attention on higher-risk areas and utilizes engagement documentation already required by PCAOB Auditing Standard No. 3, *Audit Documentation* ("AS No. 3"). Additionally, the proposed standard is designed to address smaller firm needs. For example, the proposal would allow the engagement quality reviewer to be a qualified individual outside the firm.



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II. Overview of the Proposed Standard

The proposed standard would supersede the Board's interim concurring partner review requirement.^{10/} The Board requests comments on all aspects of the proposed standard, and is particularly interested in responses to the specific questions below.

A. **Engagements for Which an Engagement Quality Review Is Required**

Under the Board's interim requirement, concurring partner reviews are to be performed in connection with audits of financial statements of SEC engagements by those firms that were members of the SECPS on April 16, 2003.^{11/} In formulating the proposal, the Board considered whether an engagement quality review should be required for all engagements performed pursuant to the standards of the PCAOB. Due to the benefits to engagement quality, the Board believes that investors and other users of financial information reasonably expect that any engagement performed according to the Board's standards should be subject to an objective review by a qualified person outside of the engagement team.

The proposed standard reflects that belief and requires an engagement quality review for all engagements performed in accordance with the standards of the PCAOB.^{12/} Such engagements include integrated audits of financial statements, audits of financial statements only, and reviews of interim financial information.^{13/}

^{10/} SECPS Requirements of Membership, Section 1000.08(f). If the Board adopts the standard, it will also make a conforming amendment to QC sec. 20 of the Board's interim quality control standards, as described in Appendix 2.

^{11/} SECPS Requirements of Membership, Section 1000.08(f).

^{12/} In contrast, the IAASB standards require an engagement quality control review to be performed for audits of financial statements of listed entities and for the firm to establish policy as to when other types of engagements should be subject to such review.

^{13/} See AU section ("sec.") 722, *Interim Financial Information*. References in this release to AU sections refer to those generally accepted auditing standards, as adopted on an interim basis in PCAOB Rule 3200T.



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Due to the benefits gained from an engagement quality review, the proposed standard also would apply to other audit and attestation^{14/} engagements performed in accordance with the standards of the PCAOB. For example, under the SEC's Regulation AB and related rules, the annual report for a class of asset-backed securities must include from each party participating in the servicing function a report regarding its assessment of compliance with certain specified servicing criteria, and an attestation report by a registered public accounting firm on that assessment.^{15/} The attestation report is to be prepared in accordance with standards on attestation engagements issued or adopted by the PCAOB.^{16/} Under the proposed standard, a registered public accounting firm would be required to obtain an engagement quality review and concurring approval of issuance to issue such an attestation report.

Finally, all registered public accounting firms – not just those that were members of the AICPA SECPS in April 2003 – would be required to comply with the proposed standard.

Questions

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?
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 required?

B. Qualifications of the Engagement Quality Reviewer

The proposed standard builds upon many of the interim requirement's provisions related to the qualifications of the engagement quality reviewer. Under the proposed

^{14/} See AT sec. 101, *Attest Engagements*, for the definition of an attest engagement.

^{15/} See Securities Exchange Act Rule 13a-18, 17 C.F.R. § 240.13a-18; Item 1122 of Regulation AB, 17 C.F.R. § 229.1122.

^{16/} See Securities Exchange Act Rule 13a-18, 17 C.F.R. § 240.13a-18.



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standard, the engagement quality reviewer may be a partner or another individual in the firm, or an individual outside the firm. As discussed below, the proposed standard notes that the reviewer is required to be independent of the client. The reviewer also must be competent, perform the assigned procedures with integrity, and maintain objectivity with respect to the engagement and the engagement team.^{17/} In addition, the engagement quality reviewer must be an associated person of a registered public accounting firm.

1. Competence

The Board's interim requirement provides, among other things, that the concurring partner should have sufficient technical expertise and experience to perform an objective review of those significant accounting, auditing, and financial reporting matters that come to the reviewer's attention, and contemplates that the reviewer possesses knowledge of relevant specialized industry practices, and SEC rules and regulations in areas pertinent to the engagement. The proposed standard seeks to establish more clearly the level of expertise and experience that is necessary to perform an objective engagement quality review. Accordingly, the proposed standard requires the reviewer to possess the level of knowledge and competence related to accounting, auditing, and financial or other reporting required to serve as the person who has overall responsibility for the same type of engagement.^{18/} For example, a person assigned to perform the engagement quality review for an audit of a public company engaged in oil and gas exploration and development should have experience sufficient to serve as the engagement partner for the audit of a public company in this specialized industry.

^{17/} Under the proposed standard, the firm's quality control policies and procedures should include provisions to provide the firm with reasonable assurance that the engagement quality reviewer has sufficient competence, independence, integrity, and objectivity to perform the engagement quality review in accordance with the standards of the PCAOB. Similarly, ISQC 1 requires that firms establish policies and procedures to address the appointment of the engagement quality control reviewer and to establish his or her eligibility through "the technical qualifications required to perform the role, including the necessary experience and authority."

^{18/} The determination of what constitutes the appropriate level of knowledge and competence should be based on the circumstances of the engagement, including the size or complexity of the business.



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Similar to the interim requirement, the proposed standard allows the engagement quality reviewer to seek assistance from others^{19/} to supplement his or her knowledge and understanding of the issues and risks related to the engagement. For example, the engagement quality reviewer might seek assistance from others when reviewing work performed in certain specialized areas. Similarly, the engagement quality reviewer may seek assistance from others to complete the review on a timely basis, such as for a large engagement. However, the engagement quality reviewer has overall responsibility for the engagement quality review and to provide concurring approval of issuance.^{20/}

2. Independence, Integrity, and Objectivity

To perform an engagement quality review under the proposed standard, the engagement quality reviewer must comply with all applicable independence requirements.^{21/} The engagement quality reviewer would also be required to maintain objectivity with respect to the engagement team and all aspects of the engagement and to perform the review with integrity.^{22/} The proposed standard would prohibit the reviewer from making decisions on behalf of the engagement team, assuming any responsibilities of the engagement team, and supervising the engagement team. The engagement quality reviewer should be able "to take a step back" and conduct the review from the perspective of an outsider "looking in."

Like the interim requirement, the proposed standard would not prohibit the engagement team from consulting with the engagement quality reviewer, and

^{19/} When the engagement quality reviewer seeks assistance from others to supplement his or her knowledge, those consulted must be independent of the client, have integrity, and possess an appropriate level of competence and objectivity.

^{20/} Concurring approval of issuance is discussed in section D.

^{21/} See, e.g., Rule 2-01(f)(7) of Regulation S-X, 17 C.F.R. § 210.2-01(f)(7) (defining "audit engagement team" to include "audit partners," and "audit partner" as certain "partner[s] or persons in an equivalent position," including the "concurring or reviewing partner"); Rule 2-01(c)(6) of Regulation S-X, 17 C.F.R. § 210.2-01(c)(6) (subjecting the engagement quality reviewer to the five-year partner rotation requirement).

^{22/} See ET sec. 102, *Integrity and Objectivity*, and ET sec. 191, *Ethics Rulings on Independence, Integrity, and Objectivity*.



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recognizes that it is often desirable that consultations take place at the time issues arise rather than at the conclusion of the engagement. In such cases, however, care should be taken not to impair the engagement quality reviewer's objectivity. To avoid impairing the reviewer's objectivity, the engagement team could, for example, develop an initial resolution of the issue prior to commencing discussions with the reviewer. If the reviewer's objectivity becomes impaired, the firm should replace the engagement quality reviewer.

Furthermore, the Board expects the engagement quality reviewer to exercise due professional care and professional skepticism without considering his or her professional status in relation to that of the engagement partner, so that the reviewer is in a position to challenge the engagement team, if necessary.

3. An Associated Person of a Registered Public Accounting Firm

The proposed standard would require the engagement quality reviewer to be an associated person of either the firm issuing the engagement report or another registered public accounting firm.^{23/} Accordingly, the reviewer could be a partner or employee of the firm issuing the report, an individual associated with another registered firm, or an individual who becomes associated with the firm issuing the report by performing the review.^{24/} A person not already associated with a firm could enter into a relationship with

^{23/} Under PCAOB Rule 1001(p)(1), an associated person of a registered public accounting firm is "any individual, proprietor, partner, shareholder, principal, accountant, or professional employee of a public accounting firm, or any independent contractor that, in connection with the preparation or issuance of any audit report – (1) shares in the profits of, or receives compensation in any other form from, that firm; or (2) participates as agent on behalf of such accounting firm in any activity of that firm; provided, however, that these terms do not include a person engaged only in clerical or ministerial tasks or a person whom the public accounting firm reasonably believes is a person primarily associated with another registered public accounting firm."

^{24/} A registered public accounting firm has an obligation to secure and enforce consents to cooperate with the Board from each associated person of the firm, see Section 102(b)(3) of the Act, including those who become associated with the firm by performing the review. The Board also may directly sanction any such person who fails to cooperate in an investigation or inspection. See Section 105(b)(3) of the Act and PCAOB Rules 5110 and 4006.



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the firm issuing the report such that the person would become associated with that firm by performing the review. Specifically, a person not already associated with a firm would become associated with the firm issuing the report if *he or she* (rather than, or in addition to, his or her firm or other employer): (1) receives compensation from the firm issuing the report for performing the review or (2) performs the review as agent for the firm issuing the report.^{25/} For example, if the firm issuing the report contracts directly with an employee of an unregistered accounting firm to perform the engagement quality review, that person would become associated with the firm issuing the report by virtue of that independent contractor relationship. Any qualified person could thus perform the review, regardless of whether he or she was associated with a registered public accounting firm before agreeing to perform the engagement quality review.

Questions

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

C. The Engagement Quality Review Process

The engagement quality review described in the proposed standard is a risk-based approach that would require the reviewer to focus on the significant judgments made by the engagement team, as well as the conclusions that the engagement team reached in forming its overall conclusion on the engagement and preparing the engagement report.

1. Scope of Review

Under the proposed standard, the engagement quality review process should include an evaluation of the significant judgments made by the engagement team and the conclusions reached in forming the overall conclusion on the engagement. To identify and evaluate the significant judgments and conclusions, the engagement quality reviewer should have discussions with the engagement partner and with other members

^{25/} See PCAOB Rule 1001(p)(1).



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of the engagement team, as necessary. This requirement to evaluate significant judgments is similar to the requirements of the related standards of the IAASB.

The proposed standard also specifies certain procedures, some of which are similar to those described in the existing requirement, that should be a part of every review process. Such procedures include, for example, evaluating engagement planning, including the judgments made about materiality and the identification of significant risks; reading the financial statements (and related disclosures), management's report on internal control, or other information that is the subject of the engagement; reviewing the engagement team's evaluation of the firm's independence in relation to the engagement; and reviewing the engagement completion document, among other things.^{26/} These procedures also are similar, in many respects, to those contained in the IAASB standards.

These procedures, however, are not a comprehensive list of all required procedures under the proposed standard. Based on these procedures (and other relevant knowledge of the reviewer), the reviewer would be required to assess whether there are areas within the engagement that pose a higher risk that the engagement team failed to obtain sufficient competent evidence or to reach an appropriate conclusion.

For the areas that pose such risk, the engagement quality reviewer should evaluate whether the engagement team performed procedures that were responsive to the assessed risks, the judgments made by the engagement team were reasonable in the circumstances, and the results of the procedures support the engagement team's conclusion. The amount of work necessary to satisfy the proposed standard's requirement would, therefore, depend on the specific risks posed by the engagement. This risk-based approach reflects the Board's belief that the engagement quality review should be rigorous enough to identify significant problems in a timely manner for correction, without imposing unnecessary costs.

^{26/} AS No. 3 requires the auditor to identify all significant findings or issues in an engagement completion document.



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Questions

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?
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?

2. Review of Engagement Documentation

The proposed standard would improve the requirements related to the engagement quality reviewer's evaluation of the engagement documentation. The Board's existing interim requirement makes reference to certain documentation to be reviewed by the concurring partner. However, the interim requirement does not explicitly direct the reviewer to evaluate whether the engagement documentation complies with audit documentation requirements or supports the conclusions reached by the engagement team. When the Board adopted AS No. 3, it stated:

First and foremost, the objectives of this audit documentation standard are to improve audit quality and to enhance public confidence in the quality of auditing and other engagements. Complete and thorough audit documentation improves the quality of the work performed in many ways. One important example is that quality audit documentation is a record of the actual work performed, which provides assurance that the auditor accomplished the planned objectives. Further, the need to document the procedures performed, the evidence obtained, and the conclusions reached demands a disciplined approach to planning and performing the engagement. Also, audit documentation facilitates the reviews performed by supervisors, managers, partners, and PCAOB inspectors.^{27/}

Accordingly, the Board believes that an important aspect of the engagement quality review should be to enhance the likelihood that the engagement team has appropriately documented its work in the areas reviewed by the engagement quality

^{27/} See *Audit Documentation and Amendment to Interim Auditing Standards*, PCAOB Release No. 2004-006 (June 9, 2004).



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reviewer. The proposed standard therefore requires the engagement quality reviewer to evaluate, for those areas reviewed, whether the engagement team's documentation supports the conclusions reached, indicates that the engagement team responded appropriately to matters that present a significant risk, and meets the documentation requirements of AS No. 3.

Question

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

3. Timing of the Review

Under the interim requirement, the concurring partner review is to be completed before release of the auditor's report. Similarly, the proposed standard requires the engagement quality reviewer to complete his or her review prior to providing concurring approval of issuance.^{28/} Beyond that, the proposed standard does not prescribe the timing of the review. The Board recognizes that the efficiency of the review can be affected by the size and complexity of the engagement and other considerations. Furthermore, the Board believes the engagement quality review could be more effective if the review is performed shortly after the engagement team's resolution of significant issues.

Question

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

D. Concurring Approval of Issuance

Under the Act, the Board's standard on engagement quality review must require a qualified person to provide concurring approval of issuance of each audit report. Accordingly, the proposed standard provides that the firm must not grant permission to the client to use the engagement report (or communicate the engagement conclusion to the client) before the engagement quality reviewer provides concurring approval. This

^{28/} Concurring approval of issuance is discussed in the following section.



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proposed requirement reflects the Board's belief that the engagement quality review should serve as a meaningful opportunity to identify problems in time to correct them.

The proposal would establish a new standard that the engagement quality reviewer must meet in order to provide a concurring approval of issuance. Under the interim requirement, the concurring partner reviewer is to conclude, based on his or her review, that no matters have come to his or her attention that would cause the reviewer to believe that the audit was not performed in accordance with the standards of the PCAOB or that the financial statements are not in conformity with generally accepted accounting principles. In contrast, the proposed standard provides that the engagement quality reviewer must not provide concurring approval of issuance if he or she knows, or should know based upon the requirements of the standard, that (1) the engagement team failed to obtain sufficient competent evidence in accordance with the standards of the PCAOB, (2) the engagement team reached an inappropriate overall conclusion on the subject matter of the engagement,^{29/} (3) the firm's report, if a report is to be issued, is not appropriate in the circumstances, or (4) the firm is not independent of its client. The Board recognizes that differences of opinion could occur between the engagement team and the engagement quality reviewer. If those differences have not been satisfactorily resolved, the engagement quality reviewer must not provide concurring approval.

This proposed requirement is intended to focus auditors on those matters that must be corrected before an audit report is issued (or before an engagement conclusion is communicated to the client). At the same time, it recognizes that the engagement quality reviewer's role is not to perform procedures amounting to a re-audit. Accordingly, under the proposed standard, the engagement quality reviewer can provide concurring approval of issuance unless he or she: (1) has actual knowledge of one of the significant problems described above, or (2) should have known of such a problem after performing the procedures required by the proposed standard.

^{29/} Inappropriate conclusions on the subject matter of the engagement would include, for example, a failure to appropriately modify the engagement conclusion in response to: (1) a material departure from generally accepted accounting principles or (2) a material weakness in internal control over financial reporting.



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Question

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

E. Documentation of an Engagement Quality Review

PCAOB inspection teams have observed apparent deficiencies in the documentation of the concurring partner review, which prevented a determination as to whether the scope of the review was appropriate and also may have contributed to the firm's failure to properly address the concurring partner's findings.^{30/} Academic research also has indicated deficiencies in documentation of the concurring partner review. For example, in recent academic research, the authors observed that "the firm's checklists or practice aids showed substantial variability. The content and extensiveness of the checklists or practice aids varied. Overall, they are not very detailed, and in most cases, are checklists that only require initials or signature of the concurring partner to indicate completion of the . . . required procedures . . ."^{31/}

The Board's interim requirement provides that the engagement documentation should contain evidence that the reviewer has complied with the firm's policies in conducting a concurring partner review, including documentation of the reviewer's conclusion. The proposed standard is more specific with regard to the documentation of the engagement quality review. Under the proposed standard, the engagement documentation should indicate:

- Who performed the review;
- The areas of the engagement subject to the review;
- The procedures performed by the reviewer;

^{30/} See PCAOB Release No. 2007-010, *Report on the PCAOB's 2004, 2005, and 2006 Inspections of Domestic Triennially Inspected Firms* (October 22, 2007).

^{31/} See Kathryn K. Epps and William F. Messier, Jr., "Engagement Quality Reviews: A Comparison of Audit Firm Practices," *Auditing: A Journal of Practice & Theory*, Vol. 26, No.2 (2007) pp.167-181.



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- When the review procedures were performed;
- The results of the review procedures; and
- Whether the engagement quality reviewer provided concurring approval of issuance.

Furthermore, the requirements related to retention of and subsequent changes to audit documentation in AS No. 3 apply with respect to the documentation of the engagement quality review under the proposed standard.

Questions

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

III. Effective Date of the Proposed Standard and Related Amendment

The Board is proposing that this standard, *Engagement Quality Review*, and the conforming amendment, be effective, subject to approval by the SEC, for engagement reports issued (or the communication of an engagement conclusion, if no report is issued) on or after December 15, 2008. Early implementation of the standard and the conforming amendment would be permitted. The Board requests comment on this proposed effective date.

IV. Opportunity for Public Comment

The Board will seek comment for a 75-day period. Interested persons are encouraged to submit their views to the Board. Written comments should be sent to Office of the Secretary, PCAOB, 1666 K Street, N.W., Washington, D.C. 20006-2803. Comments also may be submitted by e-mail to comments@pcaobus.org or through the Board's Web site at www.pcaobus.org. All comments should refer to PCAOB Rulemaking Docket Matter No. 025 in the subject or reference line and should be received by the Board no later than 5:00 PM (EST) on May 12, 2008.



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The Board will carefully consider all comments received. Following the close of the comment period, the Board will determine whether to adopt final rules, with or without amendments. Any final rules adopted will be submitted to the SEC for approval. Pursuant to Section 107 of the Act, proposed rules of the Board do not take effect unless approved by the Commission. Standards are rules of the Board under the Act.

On the 26th day of February, in the year 2008, the foregoing was, in accordance with the bylaws of the Public Company Accounting Oversight Board,

ADOPTED BY THE BOARD.

/s/ J. Gordon Seymour

J. Gordon Seymour
Secretary

February 26, 2008

APPENDIX 1 – *Proposed Auditing Standard – Engagement Quality Review*

APPENDIX 2 – *Proposed Amendment to the Interim Quality Control Standards*



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APPENDIX 1 – *Proposed Auditing Standard* – Engagement Quality Review

AUDITING AND RELATED PROFESSIONAL PRACTICE STANDARDS

Proposed Auditing Standard –

ENGAGEMENT QUALITY REVIEW





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Auditing Standard No. X

Supersedes SECPS Requirements of Membership § 1000.08(f).

Engagement Quality Review

Introduction

1. An engagement quality review and concurring approval of issuance are required for each engagement performed and completed in accordance with the standards of the Public Company Accounting Oversight Board ("PCAOB").

Qualifications of an Engagement Quality Reviewer

2. An engagement quality reviewer may be a partner of the firm that issues the engagement report (or communicates an engagement conclusion, if no report is issued),^{1/} another individual in the firm, or an individual outside the firm. The engagement quality reviewer must be an associated person of a registered public accounting firm.

3. As described below, an engagement quality reviewer must have competence, independence, integrity, and objectivity.

Note: The firm's quality control policies and procedures should include provisions to provide the firm with reasonable assurance that the engagement quality reviewer has sufficient competence, independence, integrity, and objectivity to perform the engagement quality review in accordance with the standards of the PCAOB.

4. *Competence.* The engagement quality reviewer must possess the level of knowledge and competence related to accounting, auditing, and financial or other

^{1/} An engagement report might not be issued, for example, in connection with a review of interim financial information. See paragraph .03 of AU section ("sec.") 722, *Interim Financial Information*.



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reporting required to serve as the person who has overall responsibility for the same type of engagement.^{2/}

5. *Independence, Integrity, and Objectivity.* The engagement quality reviewer must be independent of the company, perform the engagement quality review with integrity, and maintain objectivity with respect to the engagement and the engagement team.

Note: The reviewer may seek assistance from others to perform the engagement quality review. Personnel assisting the engagement quality reviewer also must be independent, perform the assigned procedures with integrity, and maintain objectivity with respect to the engagement and the engagement team.

6. To maintain objectivity, the engagement quality reviewer should not: (a) make decisions on behalf of the engagement team; (b) assume any of the responsibilities of the engagement team; or (c) supervise the engagement team. The person with overall responsibility for the engagement (e.g., the engagement partner in an audit of financial statements) remains responsible for the engagement and its performance, notwithstanding the involvement of the engagement quality reviewer.

Note: The engagement team may consult with the engagement quality reviewer on matters during the course of the engagement. When participating in such consultations, the engagement quality reviewer should not participate in a manner that would compromise his or her objectivity with regard to the engagement.

Engagement Quality Review Process

7. The engagement quality review should include an evaluation of the significant judgments made by the engagement team and the conclusions reached in forming the overall conclusion on the engagement, and in preparing the engagement report, if a report is to be issued. To identify and evaluate the significant judgments and conclusions, the engagement quality review should include discussions with the person

^{2/} PCAOB interim quality control standards describe the competencies required of a person who has the overall responsibility for an engagement (or any practitioner-in-charge of an attest engagement). See QC section ("sec.") 40, *The Personnel Management Element of a Firm's System of Quality Control-Competencies Required by a Practitioner-in-Charge of an Attest Engagement*.



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with overall responsibility for the engagement, discussions with other members of the engagement team as necessary, and other procedures, as described in paragraphs 8 and 9.

8. As part of performing the engagement quality review, the engagement quality reviewer should:

- a. Obtain an understanding of the firm's recent engagement experience with the company and risks identified in connection with the firm's client acceptance and retention process.
- b. Obtain an understanding of the company's business, significant activities during the current year, and significant financial reporting issues and risks.
- c. Review the engagement team's evaluation of the firm's independence in relation to the engagement.
- d. Evaluate engagement planning, including (1) the judgments made about materiality and the effect of those judgments on the engagement strategy and (2) the identification of significant risks, including fraud risks, and the plan for and performance of engagement procedures in response to those risks.
- e. Evaluate judgments made about (1) the materiality and disposition of corrected and uncorrected identified misstatements and (2) the severity and disposition of identified control deficiencies.
- f. Determine if appropriate consultations have taken place on difficult or contentious matters. Review the documentation, including conclusions, of such consultations.
- g. Read the financial statements, management's report on internal control, or other information that is the subject of the engagement and the engagement report (if an engagement report is to be issued) for the period covered by the engagement and for the prior period.



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- h. Read other information in documents containing financial statements that are the subject of the engagement to be filed with the SEC^{3/} and evaluate whether the engagement team has taken appropriate action with respect to material inconsistencies with the financial statements or material misstatements of fact of which the engagement quality reviewer is aware.
- i. Determine if appropriate matters have been communicated, or identified for communication to the audit committee, management, and other parties, such as regulatory bodies.
- j. Review the engagement completion document^{4/} and confirm with the person with overall responsibility for the engagement that there are no significant unresolved matters.

9. Based on the procedures performed in accordance with paragraphs 7 and 8, and other relevant knowledge possessed by the engagement quality reviewer, the engagement quality reviewer should assess whether there are areas within the engagement that pose a higher risk that the engagement team has failed to obtain sufficient competent evidence or reached an inappropriate conclusion. For the areas that pose such risk, the engagement quality reviewer should evaluate whether the engagement team performed procedures that were responsive to the assessed risks, the judgments made by the engagement team were reasonable in the circumstances, and the results of the procedures support the engagement team's overall conclusion.

10. *Evaluate Engagement Documentation.* The reviewer should evaluate whether the engagement documentation of the matters that were subject to the engagement quality review procedures –

- a. Is appropriate in the circumstances and consistent with the requirements of PCAOB Auditing Standard No. 3, *Audit Documentation* ("AS No. 3"),

^{3/} See paragraphs .02 and .04 of AU sec. 550, *Other Information in Documents Containing Audited Financial Statements*, and paragraph .18f of AU sec. 722, *Interim Financial Information*. Also, see AU sec. 711, *Filings Under Federal Securities Statutes*.

^{4/} PCAOB Auditing Standard No. 3, *Audit Documentation*, requires the auditor to identify all significant findings or issues in an engagement completion document.



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- b. Indicates that the engagement team responded appropriately to matters that present a significant risk, and
- c. Supports the conclusions reached by the engagement team with respect to the matters reviewed and the conclusions and representations in the engagement report.

11. *Timing of the Review.* The engagement quality reviewer must complete his or her review prior to providing concurring approval of issuance.

Note: The engagement quality review procedures may be performed at various points throughout the conduct of the engagement. For example, the engagement quality reviewer might review the engagement team's planning of the engagement before the engagement team implements the engagement plan. Such timely review might facilitate the effectiveness of the overall engagement.

Concurring Approval of Issuance

12. The engagement quality reviewer must not provide concurring approval of issuance if he or she knows, or should know based upon the requirements of this standard, that (1) the engagement team failed to obtain sufficient competent evidence in accordance with the standards of the PCAOB, (2) the engagement team reached an inappropriate overall conclusion on the subject matter of the engagement, (3) the firm's report, if a report is to be issued, is not appropriate in the circumstances, or (4) the firm is not independent of its client.

13. The firm must not grant permission to the client to use the engagement report (or communicate an engagement conclusion to its client, if no engagement report is issued) before the engagement quality reviewer provides concurring approval of issuance.^{5/}

^{5/} Concurring approval of issuance by the engagement quality reviewer also is required when reissuance of an engagement report requires the auditor to update his or her procedures for subsequent events. In that case, the engagement quality reviewer should update the engagement quality review by addressing those matters related to the subsequent events procedures.



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Documentation of an Engagement Quality Review

14. Documentation of an engagement quality review should be included in the engagement documentation and should include information concerning:

- a. Who performed the engagement quality review,
- b. The areas of the engagement subject to the engagement quality review,
- c. The procedures performed by the engagement quality reviewer,
- d. When the review procedures were performed,
- e. The results of the review procedures, and
- f. Whether the engagement quality reviewer provided concurring approval of issuance.

15. The requirements related to retention of and subsequent changes to audit documentation in AS No. 3 apply with respect to the documentation of the engagement quality review.



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APPENDIX 2 – Proposed Amendment to the Interim Quality Control Standards

The following proposed amendment relates to QC sec. 20 of the Board's interim quality control standards.

QC sec. 20, "System of Quality Control for a CPA Firm's Accounting and Auditing Practice"

The third sentence of paragraph 18 of QC sec. 20 is replaced with the following sentence:

These policies and procedures also should address engagement quality review pursuant to PCAOB Auditing Standard No. xx, *Engagement Quality Review*.

**Exhibit 2(a)(B)****Alphabetical List of Comments**

American Apparel & Footwear Association

American Federation of Labor and Congress of Industrial Organizations

Audit and Assurance Services Committee, Illinois CPA Society

Audit Committee, Lionbridge Technologies, Inc.

Auditing Standards Committee, American Accounting Association

BDO International

Dennis R. Beresford

John H. Biggs

Center for Audit Quality

Joseph V. Carcello

Comcast Corporation

Community Health Systems

Computer Sciences Corporation

Crowe Chizek and Company LLC

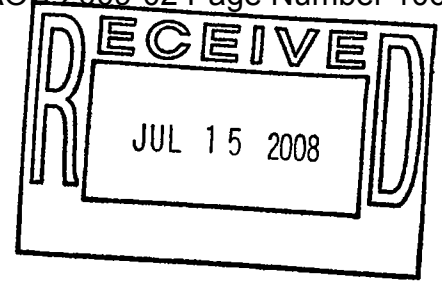
Deloitte & Touche LLP

Ernst & Young LLP

Florida Institute of CPAs

James L. Fuehrmeyer

Jeffrey S. Gilbert
Grant Thornton LLP
James H. Hance, Jr.
HealthSouth Corporation
Horwath International
Institut der Wirtschaftspruefer
KPMG LLP
Mayer Hoffman McCann PC
Mazars
McGladrey & Pullen, LLP
MetLife, Inc.
Piercy, Bowler, Taylor & Kern
PricewaterhouseCoopers LLP
Rayonier
Larry E. Rittenberg
Ross Stores, Inc.
Texas Society of CPAs
The Institute of Chartered Accountants in England and Wales
United States Chamber of Commerce
United States Government Accountability Office



July 10, 2008

Mr. J. Gordon Seymour
Office of the Secretary
Public Company Accounting Oversight Board (PCAOB)
1666 K Street, NW
Washington DC 20006

Re: PCAOB Rulemaking Docket Matter No. 025

Gentlemen,

On behalf of the American Apparel & Footwear Association (AAFA) – the national trade association of the apparel and footwear industry, and their suppliers, I am writing to submit comments on the Proposed Auditing Standard – Engagement Quality Review. While I understand these comments are being submitted after the deadline, I would ask your permission that they be considered for the record.

By way of background, AAFA has a broad membership including many public companies designing, manufacturing, importing and selling apparel and footwear products in a very competitive environment. Apparel and footwear products sold in the United States represent approximately \$370 billion of sales annually. More information on our association, and the industries we represent, is available at www.apparelandfootwear.org.

We believe a thorough engagement quality review is a necessary part of any comprehensive and credible auditing process. We note further that, per Section 103 of the Sarbanes Oxley Act of 2002, the PCAOB promulgated interim regulations in 2003 on this area that provide for such reviews. These regulations remain in force today.

We understand with this proposal that the PCAOB is attempting to improve this process to correct deficiencies in the current regulatory framework. The PCAOB has clearly identified several areas that it would like to improve with this proposal. For example, page 4 of release PCAOB 2008-002 cites an example of an engagement where inherent risks were not assessed adequately and where engagement staffing was insufficient.

While we commend the PCAOB for its efforts to address these deficiencies, we believe the proposal inadvertently causes more harm than good. It remains questionable if the proposal would in fact solve the problems – such as the one noted above – that were identified by the PCAOB.

We remain concerned that proposals to modify these regulations – as contained in the reference docket – would significantly increase audit and other costs without a corresponding increase in public confidence in the audit reports issued. These additional costs will occur at a time when public companies are feeling increased pressures on margins because of rising energy and wholesale costs and because of dampening consumer spending patterns. Increased compliance and audit costs will weaken the bottom lines of many companies, which will adversely affect investors.

A mid sized public company in our industry should expect additional audit fees approaching six figures, or more, with the full implementation of proposed standard. Bigger companies will incur even larger costs. Yet, we have been unable to quantify how these new processes will create additional public confidence in the auditing process. In fact, we believe the proposals may weaken that process.

For example, some aspects of the proposals call for duplication of the engagement team's work or for other activities that seem out of scope for the reviewers. We believe the reviewers should be focused on assessing the evaluations and work of the engagement team and in identifying any material risks that that team may have missed. Regulations that divert the attention of the reviewers into non-critical work weaken, not strengthen, this important function.

Similarly, vague requirements to maintain objectivity, while well meaning, add an extra element of confusion to what should be a predictable and straightforward process. In an effort to be compliant, review teams might refrain from the communication necessary for any properly conducted engagement quality review. Again, the end result may be a less effective and efficient process.

We are also concerned with the creation of a "know or should know" standard. We view this standard as highly subjective since reviewers, auditors, and federal regulators may all have different assessments of what any one individual "should have known." Enforcement of such a standard would be a nightmare while compliance against such a standard would be almost impossible.

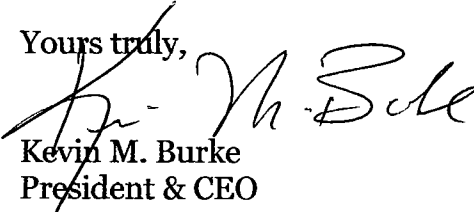
Companies should be incentivized to create auditing systems that work better, that deploy staff and resources more efficiently, and that target the risks in a more effective manner. Merely adding yet an extra layer of scrutiny, and then hobbling that extra layer with difficult-to-implement procedures, does not seem a proper solution. Additional layers only add costs, and are not necessarily

designed to uncover any problems that may exist with the initial auditing. The challenge instead should be to make the existing layers work more efficiently.

While we are pleased that the PCAOB is working to improve the current system, we strongly encourage the PCAOB not to implement the current proposal. Our members feel that the implementation of this standard will create duplicative and costly audit work that will not fix any underlying problems nor created improved investor confidence or other public benefits.

Thank you for considering our members concerns. Should you have any questions, please feel free to contact Ralph Reinecke at 703-797-9043.

Yours truly,



Kevin M. Burke
President & CEO



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Washington, D.C. 20006
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Via Electronic Mail

May 12, 2008

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

Re: PCAOB Rulemaking Docket Matter No. 025

Dear Sir or Madam,

I am writing on behalf of the American Federation of Labor and Congress of Industrial Organizations (“AFL-CIO”). Union-sponsored pension funds have over \$450 billion in assets, and benefit funds investing on behalf of union members hold in excess of \$5 trillion. The 10 million members of the AFL-CIO, their benefit funds and their unions have a vital interest in the effectiveness of public company audits.

At the time of establishment of the PCAOB, the PCAOB was granted to power to write standards for the auditing of public companies because Congress found that standards written by the auditors themselves through the AICPA had proven to be inadequate. However, as a practical matter, it was necessary at the inception of the PCAOB to readopt those AICPA standards to provide for continuity in the regulation of public company auditing. It was anticipated that the PCAOB would then review and revise those standards with an eye to strengthening them in the public interest.

For a variety of reasons this process has taken longer than anyone at the time expected. This proposed amendment to the PCAOB’s interim quality control standards in the area of engagement quality review is an important step forward in this central process of updating and strengthening the PCAOB’s auditing standards. The AFL-CIO strongly supports the proposed standard.

In particular, the proposed standard addresses the responsibility of the partner that reviews the work of the engagement partner in a public company audit. This review process is a

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critical aspect of audit quality control. Its objective should be to identify and correct audit deficiencies before the conclusion of the audit. If the process works successfully, it should address many audit problems that otherwise would have to be addressed by the PCAOB, or could lead to false and misleading financial statements, investor losses and litigation. All parties to the audit—the audit firm, the public company client, and the investing public, have a strong interest in the engagement quality review being robust and effective.

In particular, the new standard requires more than passive review of the audit by the engagement quality reviewer. It requires the reviewer to make inquiries into the audit to satisfy the requirement that the audit not be approved if there was information that the reviewer knew or should have known that evidenced either a failure on the part of the engagement team to obtain sufficient competent evidence, the drawing of an inappropriate conclusion based on that evidence, or a failure of auditor independence. This modest duty of inquiry is critical to making the engagement quality review something more than a “hear no evil, speak no evil” exercise.

Questions have been raised about the level of documentation that should be required of the engagement quality review. While it should be sufficient to inform reviewers such as the PCAOB staff, the Board should be careful not to make the engagement quality review an exercise comparable to the audit itself in formality.

The AFL-CIO appreciates the opportunity to comment on this new standard and commends the PCAOB for its work in this area.

Sincerely,

A handwritten signature in black ink, appearing to read "Damon Silvers", with a long horizontal flourish extending to the right.

Damon Silvers
Associate General Counsel



May 12, 2008

Office of the Secretary
PCAOB
1666 K Street, N.W.
Washington, D.C. 20006-2803

Re: PCAOB Rulemaking Docket Matter No. 025

Dear Sir/Madam:

The Audit and Assurance Services Committee of the Illinois CPA Society (“Committee”) is pleased to comment on the Proposed Auditing Standard, *Engagement Quality Review*.

The Committee is a voluntary group of CPAs from industry, education and public accounting. Our comments represent the collective views of the Committee members and not the individual views of the members or the organizations with which they are affiliated. The organization and operating procedures of our Committee are outlined in Appendix A to this letter.

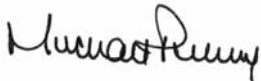
The Committee approves of the efforts of PCAOB to improve the quality of concurring reviews and established standards for its performance. However, the Committee is concerned that the standard proposed by this exposure draft is untenable. It appears that this Standard will change the requirements of a concurring partner review from a current level of negative assurance (e.g. nothing came to my attention) to that of positive assurance for all items that should have come to his/her attention during the entirety of the engagement. The use of terminology, such as “should have known” is unrealistic and could be interpreted to establish a quality role that is greater in breadth and substance than the engagement partner. We do not believe that the benefits of the positive assurance criteria set forth in the proposed standard outweigh the tremendous costs and other issues associated with its implementation.

We also have comments on certain of your questions raised by the exposure draft materials: (1) no further specificity is required, (2) an engagement quality review should be required for all audits, (3) the qualifications of a reviewer should include reasonable knowledge of the industry, economic conditions affecting the industry and appropriate experience auditing entities in the industry or similar-type industry, (4) consulting throughout the course of the audit engagement is essential so that the concurring reviewer can be involved at an early stage of the engagement, including the planning stage. We consider it imperative that every attempt be made to prevent issues from arising at the end of an engagement, when pressures to issue the auditor’s report are at their highest, (5) the reviewer should have reasonable knowledge of specific risk factors affecting the

company and the industry. It should be kept in mind that the concurring reviewer should only have limited knowledge of the company in order to maintain his independence. The proposed standard appears to be clear in stating that the concurring reviewer is dependent on his knowledge of the industry and on the planning performed by the audit team for purposes of identifying risks. He/she is not, however, in a position to be aware of risks that are not apparent from the documentation, conversations with the audit team, or knowledge of the industry, (6 thru 10) we agree with the conclusions, (12) the documentation should be consistent with the standards of AS No. 3 and should be sufficient that the quality review workpapers support the efficacy of the review.

The Illinois CPA Society appreciates the opportunity to express its opinion on this matter. We would be pleased to discuss our comments in greater detail if requested.

Sincerely,



Michael J. Pierce, CPA
Chair, Audit and Assurance Services Committee



Jon R. Hoffmeister, CPA
Vice Chair, Audit and Assurance Services Committee

APPENDIX A
ILLINOIS CPA SOCIETY
AUDIT AND ASSURANCE SERVICES COMMITTEE
ORGANIZATION AND OPERATING PROCEDURES
2007 – 2008

The Audit and Assurance Services Committee of the Illinois CPA Society (Committee) is composed of the following technically qualified, experienced members appointed from industry, education and public accounting. These members have Committee service ranging from newly appointed to more than 20 years. The Committee is an appointed senior technical committee of the Society and has been delegated the authority to issue written positions representing the Society on matters regarding the setting of audit and attestation standards. The Committee's comments reflect solely the views of the Committee, and do not purport to represent the views of their business affiliations.

The Committee ordinarily operates by assigning Subcommittees of its members to study and discuss fully exposure documents proposing additions to or revisions of audit and attestation standards. The Subcommittee develops a proposed response that is considered, discussed and voted on by the full Committee. Support by the full Committee then results in the issuance of a formal response, which at times includes a minority viewpoint.

Current members of the Committee and their business affiliations are as follows:

Public Accounting Firms:

Large: (national & regional)

Matthew L. Brenner, CPA	PricewaterhouseCoopers LLP
Jeffrey A. Gordon, CPA	KPMG LLP
Jon R. Hoffmeister, CPA	Clifton Gunderson LLP
Neil F. Finn, CPA	Deloitte & Touche LLP
William P. Graf, CPA	Deloitte & Touche LLP
James P. McClanahan, CPA	McGladrey & Pullen LLP
Gary W. Mills, CPA	BDO Seidman, LLP
Michael J. Pierce, CPA	McGladrey & Pullen LLP
Kevin V. Wydra, CPA	Crowe Chizek and Company LLC

Medium: (more than 40 employees)

Damitha N. Bandara, CPA	Blackman Kallick LLP
Sharon J. Gregor, CPA	Selden Fox, Ltd.
Stephen R. Panfil, CPA	Bansley & Kiener LLP
Jennifer E. Sanderson, CPA	Frost, Ruttenberg & Rothblatt, P.C.

Small: (less than 40 employees)

Scott P. Bailey, CPA	Bronner Group LLC
Loren B. Kramer, CPA	Kramer Consulting Services, Inc.
Andrea L. Krueger, CPA	Corbett, Duncan & Hubly P.C.
Ludella Lewis, CPA	Ludella Lewis & Company
Richard D. Spiegel, CPA	Steinberg Advisors, Ltd.

Industry:

James R. Adler, CPA	Adler Consulting Ltd.
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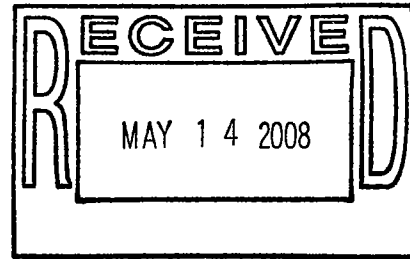
Educator:

Simon P. Petravick, CPA	Bradley University
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Staff Representative:

Paul E. Pierson, CPA	Illinois CPA Society
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Audit Committee
Lionbridge Technologies, Inc.
1050 Winter Street, Suite 2300
Waltham, MA. 02451



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

RE: New Proposed Standard – Engagement Quality Review

Dear PCAOB,

We are pleased to have the opportunity to comment on the proposed draft by the PCAOB regarding audit engagement quality.

First, we applaud the PCAOB's governance oversight and its initiative to improve the quality of audit engagements. However, we also have many concerns, not on the intent of this new proposal, but on its implementation and interpretation as currently written.

While most audit firms already have a quality engagement process and strict rules for monitoring by the concurring partner, the proposed new standard seems to imply a much more rigorous exercise which could create delays in filings and significant unnecessary burdensome costs on companies without any value added.

We would strongly encourage the PCAOB to re-examine the implications of this new policy, its cost and the practicality of implementing the standard in an organized and cost effective manner for 2008 and include examples of reasonable efforts for a concurring partner to assess risk and compliance.

Our experience with a major 'Big 4' audit firm today seems to work well. We are familiar with their engagement quality guidelines and their concurring partner involvement and do not believe there should be any additional burdensome costs on our company or potential delays in public reporting due to any extreme or literal interpretation of the new rule.

Respectfully,

A handwritten signature in black ink, appearing to read "E. Blechschmidt".

Edward A. Blechschmidt
Chairman, Audit Committee
Lionbridge Technologies, Inc.

May 12, 2008

Office of the Secretary
Public Company Accounting Oversight Board
1666 K Street, N.W.
Washington, D.C. 20006-2803

Via email to comments@pcaobus.org

RE: PCAOB Rulemaking Docket Matter No. 025: Proposed Auditing Standard - Engagement Quality Review.

Dear Board Members:

The Auditing Standards Committee of the Auditing Section of the American Accounting Association is pleased to provide comments on the *PCAOB Rulemaking Docket Matter No. 025: Proposed Auditing Standard - Engagement Quality Review*. We very much appreciate the opportunity to provide input.

The views expressed in this letter and attachments are those of the members of the Auditing Standards Committee and do not reflect an official position of the American Accounting Association. In addition, the comments reflect the overall consensus view of the Committee, not necessarily the views of every individual member.

We hope that our attached comments and suggestions are helpful and will assist in finalizing the proposed guidance. If the Board has any questions about our input, please feel free to contact our committee chair for additional follow-up.

Respectfully submitted,

Auditing Standards Committee
Auditing Section - American Accounting Association

Committee Members:

Chair – Thomas M. Kozloski, Wilfrid Laurier University, tel: 519-884-0710 ext. 2679,
int: tkozloski@wlu.ca

Past Chair - Robert D. Allen, University of Utah
Vice Chair – Randal J. Elder, Syracuse University
Ed O'Donnell, University of Kansas
Robert J. Ramsay, University of Kentucky
Sandra Shelton, DePaul University
Jay Thibodeau, Bentley College

Auditing Standards Committee
Auditing Section – American Accounting Association

General Comments

The Committee commends the PCAOB (“the Board”) for proposing an audit standard relating to engagement quality review. We believe that in general the proposed standard sets the proper tone and maintains the proper balance as it strengthens the existing guidance in this area of practice. In the Committee’s opinion, this standard will assist practitioners in meeting the Board’s objective for guidance in this area: increasing the likelihood of identifying and correcting deficiencies in the planning, execution, and wrap-up of the audit engagement prior to the issuance of the auditor’s report. The Committee believes that, for most accounting firms, the proposed standard will assist practitioners in accomplishing this objective without the incurrence of excess or burdensome additional costs. In short, it is our opinion that the proposed standard will result in more effective audits.

The following section presents a number of specific comments or suggestions relating to the proposed standard, organized along the lines of the questions posed by the Board in the body of the guidance preceding the draft of the proposed standard.

Comments Addressing PCAOB-proposed Questions

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 the objective?

The Committee agrees with Board Member Charles Niemeier that the standard should state an objective. The Board has articulated an objective in the release (and related materials) regarding engagement quality review, without necessarily calling it such. Based on the guidance, it would seem that the objective of the proposed standard is (as stated above in “General Comments”): to increase the likelihood of identifying and correcting deficiencies in the planning, execution, and wrap-up of the audit engagement prior to the issuance of the audit report. Another way of presenting the objective, or an additional objective, framed in a less “negative” manner than focusing on the detection of deficiencies, might be: to ensure that the engagement complies with PCAOB standards and the audit firm’s own quality control standards. Even though these objectives are implied in the proposed standard, the Committee believes that explicitly presenting the objective(s) early in the standard will provide additional focus to the standard.

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 required?

The Committee believes that engagement quality reviews should be performed for all engagements performed in accordance with the standards of the PCAOB. Specifically, we believe that applying the proposed standard to reviews of interim financial

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information will result in more effective interim reviews, and therefore more effective audits. In support of this assertion, the Committee cites research that indicates that fraudulent financial reporting often begins in an interim period, with additional actions taken at year end (Beasley, et al., 1999).

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

The proposed standard provides flexibility as to who conducts the review, and sets an appropriate benchmark for the technical qualifications of the reviewer (i.e., the ability to function as an engagement partner on the audit of a similar entity). In the areas of independence and objectivity, however, it may be difficult for the engagement quality reviewer to challenge the decisions and actions of the engagement team if the reviewer does not have sufficient authority relative to the engagement partner. For instance, if the engagement partner of an audit is the partner-in-charge of a particular office of the firm, it may be advisable for the reviewer to come from another office of the firm. However, as noted in paragraph 3 of the proposed standard, specific guidance as to how a particular firm resolves these issues could be addressed in the firm's quality control standards.

4. Should the proposed standard allow the engagement team to consult with the engagement quality reviewer during the engagement? Would such a consultation impair objectivity?

This is a difficult and very critical issue. On the one hand, consultation provides for efficiency in the conduct of the audit. On the other hand, engagement quality reviewers may not be sufficiently objective to make final determinations or judgments that go against their earlier advice provided in the consultation.

The Committee believes that consultation with the engagement quality reviewer may be particularly useful in planning (especially risk assessment, and the planned response to identified risks). As to unexpected and significant matters that arise during the conduct (testing phase) of the engagement, the proposed standard might include language that directs consultations regarding these matters first to other persons and resources in the accounting firm, and then to the engagement quality reviewer, as a last source of consultation.

If the Board decides that consultation with the engagement quality reviewer is appropriate, the Committee believes that the reviewer should not consult with the engagement team about an issue, whether it involves the planning, execution, or wrap-up of the audit, until the engagement team has first determined its own position on that issue. Numerous research studies in decision-making have found that decision-makers are susceptible to confirmation bias. Auditors in the setting of professional practice have been found to be likewise susceptible (Bamber, et al., 1997; Church, 1990). The implication of this research for engagement quality reviewers is that reviewers may not

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be objective relating to the decisions and judgments in which they have formerly participated. Libby and Trotman (1993) note that “there are systematic offsetting differences in the manner in which initial decision makers and reviewers attend to information which ensure that evidence inconsistent with initial judgments is given adequate consideration. The review process can act as an effective control by increasing the chances that the implications of inconsistent evidence are considered.” Specifically, “initial decision makers’ judgments resulted in a tendency for their relative recall to be in the direction of information consistent with their judgments, while initial decision makers’ judgments resulted in the reviewers’ relative recall being in the direction of information inconsistent with that decision.”

Therefore, the concern is that engagement quality reviewers who are involved in decisions will tend to remember information consistent with the decision. However, if they act only as reviewers, and not decision makers, they will consider more information that is inconsistent with the decision, which may enhance the quality of the overall review.

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

In general, the Committee considers the scope and extent of the engagement quality review procedures included in the proposed standard to be appropriate, but we offer the following suggestions.

The standard is silent on a process for the resolution of disagreements between engagement partner and reviewer. We believe that it may be useful to include language in the proposed standard that requires the firm to have such a process in place as part of the firm’s quality control standards.

Also, it may be useful to include language in the proposed standard that indicates that the procedures in para 7, 8 and 9 must be performed, but the auditor is not necessarily limited to those procedures. In addition, since the evaluation of the engagement documentation is one of the duties and responsibilities of the reviewer, it may be useful to incorporate the substance of para 10 into the list in para 8, with para 9 presenting the “wrap-up and evaluate” guidance as it does already.

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?

The Committee believes that a risk-based approach is appropriate, but the risk-based approach is not well-described. Auditors’ standard methodology for evaluating risk is the risk-model, but it is not clear that is what is intended here. For example, auditors have been criticized for not gathering sufficient evidence on “high risk” engagements. How

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should the engagement quality review differ on such engagements? Should the engagement quality reviewer evaluate procedures for all identified inherent risks, or all fraud risks, or all significant risks (a term used but not defined on p. 15, which could be defined as inherent and control risk combined)? Are there evidential risks that are separable from inherent and fraud risks?

For example, many frauds arise from revenue recognition issues such as channel stuffing and side agreements with customers. These are clearly inherent and/or fraud risks which influence the nature of the evidence gathered. We suggest that the term “significant risk” be defined in the standard and that the engagement quality reviewer be required to evaluate whether the evidential matter to be gathered and evaluated is sufficient and competent to address each significant risk.

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

The Committee believes this is another critical and difficult issue. The release refers to academic research that indicates the reviews have mostly consisted of checklists. However, it is important to note that the reviewer reviews, rather than performs detailed, evidence gathering procedures, which is why the checklist may be used to guide and possibly document the work of the reviewer.

It seems based on the discussion in the release that the Board would like to provide guidance that would lead practitioners to move away from a checklist and sign-off approach, with little or no additional documentation behind the checklist or decision aid concerning the particulars of what the reviewer did in conducting the review. The Committee believes that the guidance provided in the proposed standard will likely accomplish this objective.

References

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Beasley, M., J. Carcello, and D. Hermanson, (1999). Fraudulent financial reporting: 1987-1997. An analysis of U.S. public companies. COSO/AICPA: Research report.

Church, B. (1990). Auditors’ use of confirmatory processes. *Journal of Accounting Literature*. Gainesville: Vol. 9; p.229.

Libby, R. and K. Trotman. (1993). The review process as a control for differential recall of evidence in auditor judgments. *Accounting, Organizations, and Society*. Oxford: Aug. Vol. 18, Iss. 6; p.559.



COMMENT LETTER

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

Date
9 May, 2008

By email - comments@pcaobus.org

Dear Sirs,

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

We are pleased to have this opportunity to comment on the PCAOB’s proposed auditing standard, *Engagement Quality Review and Conforming Amendment to the Board’s Interim Quality Control Standards* (the Proposed Standard) on behalf of BDO International.¹

We support the PCAOB’s efforts to strengthen the quality of the existing second partner review process. Such a process, when soundly implemented, provides an effective mechanism to enhance the quality of the audit and the consequent reliability of financial reporting. In that regard, we believe that the process would be further strengthened on a consistent global basis through convergence with the standards proposed by the International Accounting and Assurance Standards Board (“IAASB”) in this area, such as the Proposed Redrafted International Standard on Auditing (“ISA”) 220, *Quality Control for an Audit of Financial Statements*, and the 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*.

Our responses to the specific questions posed in the Release are set forth below. They are intended to promote greater clarity of the final standard.

A. Engagements for Which an Engagement Quality Review is Required

- 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?**

We believe that the Proposed Standard would benefit from an explicitly stated overall objective of the engagement quality review. Providing such an overall objective supports the principles based audit approach, which requires the auditor to step back and evaluate whether the procedures performed were sufficient in meeting the objective, and serves to avoid a “checklist mentality.”

¹BDO International is a world wide network of public accounting firms, called BDO Member Firms, serving international clients. Each BDO Member Firm is an independent legal entity in its own country.

In determining the language for such objective, we recommend considering as a starting point paragraph 20 of Proposed Redrafted ISA 220, which states that a quality control review should provide:

“...an objective evaluation of the significant judgments made by the engagement team, and the conclusions reached in formulating the auditor’s report.”

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 required?

We believe that an engagement quality review should be required for all engagements performed in accordance with the standards of the PCAOB based on the rationale expressed in the Proposed Standard that *well-performed engagement quality reviews are an important element in establishing a basis for investor reliance.*

B. Qualifications of the Engagement Quality Reviewer

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

One aspect of the qualifications of an engagement quality reviewer as described in the proposed standard is not clear to us, in that it states that an engagement quality reviewer may be a partner or *another individual in the firm or an individual outside the firm.* This seems to conflict with Section 103 of the Sarbanes-Oxley Act of 2002 (the “Act”), which requires the Board to include in the auditing standards a requirement that “each registered public accounting firm shall provide a concurring or second partner review...” (Emphasis added). There is similar language in Section 203 dealing with lead and concurring partner rotation. Our understanding of these provisions of the Act is that the engagement quality review must be performed by a partner. Rule 2-01 of Regulation S-X also uses the term “partner” when referring to the “concurring partner.” Regulation S-X uses the term “...partner or persons in an equivalent position...” when defining an audit partner. In practice, we believe that “principals” would be in an equivalent position within a firm, but only if they have authority to bind the firm. We do not believe that this equivalency would extend to those below a principal role, such as a senior manager. While we do not object to extending the capability to perform the engagement quality review beyond the pure partner role, provided that the individual has the requisite other qualifications, we suggest that the final standard reconcile the qualifications of the reviewer with the aforementioned provisions of the Act and Regulation S-X.

The Proposed Standard requires the engagement quality reviewers, including non-partners, to possess *the level of knowledge and competence related to accounting, auditing, and financial reporting to serve as the person who has overall responsibility for the same type of engagement.* Ordinarily, an individual possessing these characteristics would be a partner (or principal) or someone who has the *authority* to act as an audit engagement partner. This characteristic is included in Proposed Redrafted ISA 220 (paragraph A42) and, in our view, reflects a substantive factor in evaluating the ability of the engagement quality reviewer to stand up to the engagement partner when difficult issues arise. Assuming it is permissible under the Act and Regulation S-X for suitably qualified non-partners to perform an engagement quality review, it seems to us, therefore, that this Proposed Standard or the Quality Control Standards should provide that when a non-partner performs the review, the working papers should contain documentation about how the firm’s quality control standards

ensured that such person was appropriately qualified, considering criteria such as the independence and technical qualifications, experience, and authority of the reviewer.

To clarify the Board's intention regarding the meaning of the terms partner, engagement partner, practitioner-in-charge, and engagement quality reviewer, we suggest including a definition section within the standard. While these terms are used extensively within the accounting profession, they may have different meanings to different people. We suggest that, wherever possible, such definitions should be generally consistent with those set out in the proposed redrafted ISQC 1, included below.

Engagement partner – The partner or other person in the firm who is responsible for the engagement and its performance, and for the report that is issued on behalf of the firm, and who, where required, has the appropriate authority from a professional, legal or regulatory body.

Engagement quality control reviewer – A partner, or other person in the firm, suitably qualified external person, or a team made up of such individuals, none of whom is part of the engagement team, with sufficient and appropriate experience and authority to objectively evaluate the significant judgments the engagement team made and the conclusions they reached in formulating the report.

Partner – Any individual with authority to bind the firm with respect to the performance of a professional services engagement.

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?

While we agree that it is important for the engagement quality reviewer to maintain his or her objectivity, we believe that recognition should be given to practical circumstances that would make it reasonable to permit engagement teams to consult with the engagement quality reviewer at the time issues arise. This is particularly the case for smaller firms where technical experts are limited in number and most also perform client service roles, such as serving as engagement quality reviewers.

We understand the concept that for an engagement quality reviewer to remain objective, the engagement team should ordinarily develop a view on issues prior to consultation. However, we believe that in practice there may be some situations, either because of timing or resource constraints, where the engagement team may not form a view on a highly specialized or technical issue prior to consultation with the engagement quality reviewer. In our view, sporadic consultations in this fashion would not ordinarily impair the reviewer's objectivity with respect to the overall engagement, or necessitate his or her replacement on the engagement.

C. The Engagement Quality Review Process

1. Scope of Review

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?

Generally, we agree that the descriptions of the scope and extent of engagement quality review procedures are appropriate. However, there are some areas where we believe additional clarification is needed as to the nature and extent of the review, as follows:

Review of working papers

We believe the Proposed Standard is unclear as to whether or not the review ordinarily would extend to the detailed working papers supporting the judgments made and conclusions reached in the higher risk areas, or whether this evaluation can be achieved through review of the top memorandum, discussions with engagement teams, and performing the specific procedures in paragraph 8.

We believe that the requirement set out in paragraph 10.a. that requires the reviewer to evaluate the engagement documentation of the matters that were subject to the review should ordinarily require the reviewers to review the important detailed working papers in the areas subject to significant judgment. However, we believe this requirement as presently worded could be read as meaning that the reviewer need only ensure that the items specified in paragraph 8, rather than the underlying working papers themselves, are documented in accordance with Auditing Standard No. 3 (“AS No. 3”).

As such, we recommend clarifying the intended extent of the engagement quality review, and specifically stating that ordinarily a review of selected working papers evidencing the procedures performed and conclusions reached for the higher risk areas is required, although the extent of such review would vary based on an assessment of risk. This approach is consistent with the proposed redrafted ISQC 1, which provides for such a review of selected working papers relating to the significant judgments made and conclusions reached. (Refer to paragraphs 44 and 45 of proposed redrafted ISQC 1.)

Significant Risks

The term “significant risk” is used in the Proposed Standard to refer to a matter the reviewer should assess as part of the evaluation of engagement planning. This term has a specific meaning within the AICPA Statements on Auditing Standards (“SAS”) 109, *Understanding the Entity and its Environment and Assessing the Risks of Material Misstatement* (which is similar to the ISA equivalent standard) and is defined as follows:

As part of the risk assessment described in paragraph 102, the auditor should determine which of the risks identified are, in the auditor’s judgment, risks that require special audit consideration (such risks are defined as “significant risks”). Paragraphs 45 and 53 of SAS No. 110 describe the consequences for further audit procedures of identifying a risk as significant.

However, this term, “significant,” which in the AICPA standard is not necessarily synonymous with “high” or “higher,” is not defined in the PCAOB’s auditing standards, and for clarity purposes, we suggest that a different term be used.

Review of Interim Financial Information

We agree that an engagement quality review and concurring approval of issuance are appropriate for each engagement performed and completed in accordance with PCAOB standards, including reviews of interim financial information where an engagement report may not be issued. However, we believe that certain of the required procedures set out in the Proposed Standard may not be applicable to a review of interim financial information in

accordance with AU section 722. For example, paragraph 8.d. (2) requires the engagement quality reviewer to evaluate engagement planning, including the identification of significant risks, including fraud risks, and the plan for and performance of engagement procedures in response to those risks, but this evaluation is not applicable to an interim review. As such, we recommend identifying those procedures that may not be applicable to such a review.

- 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 a risk based approach to the engagement quality review. However, the Proposed Standard does not clearly define the meaning of the phrase “areas within the engagement that pose a higher risk.” As such, we recommend that the focus of the engagement quality review be on those areas that pose a higher risk of material misstatement to the financial statements or, where applicable, a risk of material weakness in internal control over financial reporting.

2. Review Engagement Documentation

- 7. Are the proposed requirements for the review of the engagement team’s documentation appropriate? If not, how should they be changed?**

As described in our response to question 5, we believe the proposed requirements should be clarified with respect to the depth of the working paper review and, as such, we recommend providing additional guidance on this matter based on the suggestions contained in that response. In that regard, it is also not clear whether (1) the reviewer is simply required to evaluate the procedures performed by the engagement team based on what they have documented in the working papers and consider whether that documentation complies with the provisions of AS No. 3 (which we believe is the appropriate approach) or (2) in any review of analyses in detailed working papers, the engagement quality reviewer is expected to re-perform any procedures documented on such working paper and/or tie information back to underlying accounting records or other documents.

3. Timing of the Review

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

We agree with the description of the timing of the engagement quality review, as set forth in the Proposed Standard.

D. Concurring Approval of Issuance

- 9. Is the standard for the engagement quality reviewer’s concurring approval of issuance appropriate? If not, how should it be changed?**

We believe that the requirement in the Proposed Standard for an engagement quality reviewer’s concurring approval of issuance is appropriate and we support the PCAOB’s focus on strengthening the provisions within the standard to ensure that those matters that must be corrected before an audit report is issued, or before an engagement conclusion is communicated to the client (if no engagement report is issued), are handled appropriately.

However, the form of such approval should recognize that the engagement quality reviewer's responsibility is not the equivalent of the engagement partner. Without first-hand knowledge of the client's business environment, the benefit of discussions with management and other client personnel, the opportunity to review client documents or controls, or the ability to observe the client's actions or attitudes, an engagement quality reviewer generally is not in the same position to make informed judgments on significant issues as would be expected of the engagement partner. Therefore, to avoid any confusion, we believe the standard should provide a clear distinction between the roles and responsibilities of each such that it clearly states that notwithstanding the procedures performed by the engagement quality reviewer, the engagement partner has final responsibility for the audit engagement, including whether the auditor's report is appropriate in the circumstances. This different level of responsibility of the engagement quality reviewer caused by the inherent limitation of his or her breadth of knowledge about the issuer seems more appropriately suited to negative assurance. This form of assurance is already included in Interim Standard AU722, *Interim Financial Information*, in which less than full assurance is contemplated.

In contrast, we believe that the phrase "should know based on the requirements of this standard" may have unintended consequences. This is primarily because this term is not defined within the professional standards, and outside parties may attribute a higher level of assurance to this than is warranted by the application of the procedures provided for in the Proposed Standard. As a result, reviewers who are concerned about being second guessed as to what they "should know" may feel compelled to perform additional procedures that are not contemplated by the Proposed Standard.

We therefore suggest that the Proposed Standard adopt terminology already available in the professional standards that will also more closely align with the International Standards in this area. Suggested wording is as follows:

"The engagement quality reviewer should perform the procedures set out in this standard. The reviewer should not provide concurring approval if, as a result of these procedures, anything comes to his/her attention [or he/she is aware of anything] that would cause him/her to believe that"

We further recommend providing additional guidance with respect to a mechanism for the resolution of disagreements between the engagement partner and the engagement quality reviewer. This guidance should require any conclusions reached to be documented in accordance with the provisions of AS No. 3, paragraph 8, and that the report not be issued until the matter is resolved in accordance with a firm established framework for the resolution of such differences that reflects an ultimate decision by a suitable technically qualified partner within the firm.

Additionally, we note that paragraph 13 of the Proposed Standard provides guidance to a firm in fulfilling its responsibility to ensure that reports issued are appropriate in the circumstances and, as such, this guidance would seem better placed within the quality control standards. However, footnote 5 to this paragraph remains appropriate, and we therefore suggest that the current wording of paragraph 13 be replaced with wording based on the information in footnote 5, as the footnote information is more pertinent to procedures a reviewer should perform.

E. Documentation of an Engagement Quality Review**10. Are the documentation requirements for an engagement quality review appropriate? If not, how should they be changed?**

Generally, we believe that the documentation requirements for an engagement quality review are appropriate. However, we suggest clarification of the nature and extent of the documentation of procedures performed by the engagement quality reviewer to ensure consistency in practice. For instance, item 14.c. requires documentation of the procedures performed, but the form of that documentation is not clear and without additional clarity, the level of documentation may be excessive. Given the guidance in the Proposed Standard, documentation could range from a simple sign off on the working paper (which we believe is the appropriate approach) to something much more in depth, such as the preparation of a summary memo describing exactly what the reviewer looked at on the working paper. Additionally, item 14.e. requires the results of the review procedures to be documented; however, once again the nature of the required documentation is not apparent. It is not clear whether this documentation requirement could be satisfied simply by providing concurring approval of issuance (which we believe is the appropriate approach), or whether something more is contemplated.

We also suggest that guidance be provided along the lines of AS No. 3, paragraph 6, which indicates that the identification of who performed the review and when that review took place may necessitate having the reviewer initial and date specific working papers rather than include a general description of the areas covered by the review.

11. 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?

As noted in our response to Question 9 above, we believe that the Proposed Standard should require documentation of the resolution of any disagreements between the engagement partner and the engagement quality reviewer.

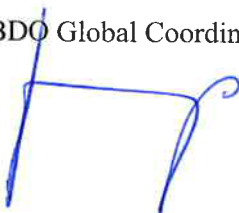
Effective Date

To allow all registered public accounting firms sufficient time to incorporate the guidance included within the final standard into their engagement quality reviews, we recommend that the effective date be no earlier than for periods *beginning* on or after six months after the standard is approved by the Securities and Exchange Commission.

We would be pleased to discuss any questions you may have about our comments. Please contact Helen Thomson at +32 (0)2 778 0130 or via electronic mail at hthomson@bdoglobal.com with any questions.

Yours faithfully,

BDO Global Coordination B.V.



March 7, 2008

Office of the Secretary
PCAOB
1666 K Street, NW
Washington, DC 20006-2803

PCAOB Rulemaking Docket Matter No. 025

Dear Secretary:

This letter includes my comments on PCAOB Rulemaking Docket Matter No. 025, "Engagement Quality Review." As noted in the proposal, this proposal mainly updates and formalizes the Board's Interim Quality Control Standards with respect to a requirement for concurring partner reviews. As such, the principal objective seems to be to extend the concurring partner review requirement to certain smaller accounting firms that weren't previously members of the AICPA's SEC Practice Section. This is an appropriate step to ensure reasonably consistent quality controls for the audits of all public companies. As such, I concur with the basic conclusions of the proposal. However, I have two matters for your consideration.

Paragraph 9 of the proposed rule states that "Based on the procedures performed in accordance with paragraphs 7 and 8, and other relevant knowledge possessed by the engagement quality reviewer, the engagement quality reviewer should assess whether there are areas within the engagement that pose a higher risk that the engagement team has failed to obtain sufficient competent evidence or reached an inappropriate conclusion." This strikes me as overly broad as nearly any area of an audit might involve insufficient evidence or inappropriate conclusions, and this won't necessarily be clear from the procedures in paragraph 8. One result may be that concurring partners feel it necessary to repeat a high percentage of the review work of the engagement partner, resulting in unnecessary costs

and perhaps a delay in finalizing year end audits. Another result may be that PCAOB inspectors, having reviewed all of an engagement's working papers, may find fault with the more limited work of a concurring partner because they think he or she should have looked at areas they found deficient through their comprehensive inspection. Neither of these seems to be a positive outcome.

The best way to address this problem would be to simply eliminate paragraph 9 as paragraphs 7 and 8 specify both the overall approach and specific procedures that are to be followed by the concurring partner reviewer. However, it may be possible to address the problem by expanding on paragraph 7 to clearly state what the objective of the concurring partner review is. The present draft of the standard does not specify what is supposed to be accomplished by the concurring partner review and that seems like a glaring omission.

Another matter for your consideration is the relationship of the concurring partner review and the company's audit committee. At a minimum, I believe that the standard should encourage accounting firms to clearly communicate with audit committees on the purpose and timing of this review. In my experience on audit committees, I've found that accounting firms don't normally say much about the independent review unless I ask about it. As a best practice, I think the reviewer should meet with the audit committee at least once a year and his or her role should be explained. Otherwise, there's a chance that a last minute problem or delay in the audit can occur because of concerns expressed by the reviewer without the audit committee even knowing that this procedure has to be performed.

Please let me know if you'd like to discuss my comments.

Sincerely,

Dennis R. Beresford
Ernst & Young Executive Professor of Accounting

780 Third Avenue
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JOHN H. BIGGS
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Chief Executive Officer
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May 7, 2008

Mr. Mark Olson
Chairman
Public Company Accounting Oversight Board
1666 K Street NW
Washington, DC 20006-2803

Dear Mark:

I had a brief conversation with you and Bill Gradison about my concerns on the language in the proposed Auditing Standard #7. We had a Boeing board meeting last week and I had a chance to go over the issues with my fellow Audit Committee members. They encouraged me to write a letter to you expressing our views.

I have been chairman of the Boeing Audit Committee during the entire period of implementation of Section 404. Given my past interest in this subject and my experience at JPMorganChase and Boeing, I did get a good view of how the process worked.

We believe at Boeing that very substantial improvements in the controls of the company have occurred as a result of our significant and very expensive efforts. The direct costs for Boeing itself were extremely high as were the extra charges by our external auditor for their role.

On balance I think I can speak for all of us as saying it was a good thing to have imposed on us but that the implementation was very expensive and that there were some unnecessary expenses due to the very broad interpretations of Auditing Standard #2.

We believe many of these extra costs were not intended or anticipated by the PCAOB.

We have made substantial recovery in our expense levels as the compliance with AS5 becomes "business as usual" and our auditor has been able to bring down their costs.

Mr. Mark Olson

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All this is by way of preamble for my unusual position as a member of your Advisory Committee and also chairman of a prominent company's auditing committee in urging caution on some of the language in the proposed Auditing Standard #7.

First off the date is extremely awkward and of real concern for us. We have already developed our audit plan for 2008 with its fee structure and do not quite know what to make of the additional costs we should prepare for the concurring auditor.

Our time tables for our 2008 press releases and SEC filings are fairly firmly set. If changes in the concurring review process were to cause a delay in the completion of our auditors' work, we expect it would be quite difficult to adjust our related schedules for the release of our financial information.

Many of the provisions of the Standard are understandable and seem to me not controversial.

However, the standard for the concurring auditor or "engagement quality reviewer" seems significantly different from what has been expected in the past. I am sure you are aware of this difference.

As I see it, the old standard focused on the concurring auditor examining closely the work product of the audit team with primary responsibility. This appeals to me as a kind of real time quality "peer review".

The proposed standard however, goes conceivably much farther than this with the phrase "concurrent partner has to have knowledge of matters that 'he or she knows or should know rather than matters that have come to his/her attention'".

I note that in every audit blowup that I am aware of, the "should have known" language is very prominent in lawsuits and media comment.

I would think someone considering a rule as a concurring partner would wonder what responsibility has been placed on him with this new language. The implications of that I am sure are obvious to all of you at the PCAOB.

For instance does the concurring partner have to be supported in a much more elaborate way to find out those things that "he should have known"? Is this language somehow more far reaching than the basic obligation of the audit firm

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and primary partner? Also does this pose very severe problems for a small audit firm in finding an outside person to become the reviewing partner?

I would think that the basic purpose of the concurring partner is part of the process by which firms and the PCAOB can improve the internal quality controls of the auditing firms. I would not think its purpose is to extend the responsibility overall of the firm or of individuals within it—that responsibility is already quite broad.

The language on documentation seems reasonable to me but our colleagues at Deloitte & Touche have concerns which I am sure they will express directly to you.

I express these views on behalf of the Boeing Audit Committee and myself in this spirit of supporting the goals we have all had for the PCAOB in ensuring high quality audits. We need them as much now as we did at the time of the hearings at Senator Sarbanes' committee on the need for the Sarbanes-Oxley legislation. We are not in the camp of those who seek to roll back the important protections investors have received through the creation of the PCAOB.

As I said frequently to you and others of my colleagues in business, I believe the PCAOB is doing exactly the job all of us who were advocates of Sarbanes-Oxley hoped for.

Sincerely,



John H. Biggs



May 12, 2008

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

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RE: Request for Public Comment on PCAOB's Proposed Auditing Standard – *Engagement Quality Review and Conforming Amendment to the Board's Interim Quality Control Standards*; PCAOB Rulemaking Docket Matter No. 025

Dear Office of the Secretary:

The Center for Audit Quality (CAQ or the Center) is an autonomous public policy organization serving investors, public company auditors and the capital markets and is affiliated with the American Institute of Certified Public Accountants (AICPA). The CAQ's mission is to foster confidence in the audit process and aid investors and the markets by advancing constructive suggestions for change rooted in the profession's core values of integrity, objectivity, honesty and trust. Based in Washington, D.C., the CAQ consists of nearly 800 member firms that audit or are interested in auditing public companies. We welcome the opportunity to share our views on the Public Company Accounting Oversight Board's (PCAOB or the Board) proposed auditing standard – *Engagement Quality Review (EQR) and Conforming Amendment to the Board's Interim Quality Control Standards* (the proposal or proposed standard).

We strongly support auditing standards that promote audit quality and believe that a robust and effective engagement quality review that focuses on significant judgments made and conclusions reached by the engagement team furthers that purpose. We also strongly support the Board's proposal that all registered public accounting firms – not just those that were members of the AICPA SEC Practice Section as of April 16, 2003 – be required to comply with the engagement quality review standard. We believe that requiring all firms to comply is consistent with the Board's

directive under Section 103 of the Sarbanes-Oxley Act of 2002 and is in the public interest.

However, we are concerned that the proposed standard goes well beyond international auditing standards promulgated by the International Auditing and Assurance Standards Board (as well as the Board's current interim standard),¹ and that the resulting incremental effort will not have a commensurate benefit to audit quality. Specifically, as discussed in greater detail below, our concerns are directed to the following fundamental aspects of the proposed standard and its divergence from international auditing standards:

- The standard does not contain an objective that articulates the purposes and objectives of the review;
- The standard establishes a new standard of performance for the engagement quality reviewer (“know or should know”) that is likely to result in the performance of substantial additional procedures and engagement quality reviewers being overly focused on being second-guessed as to what they should have known;
- The standard requires independent evaluations by the engagement quality reviewer, rather than reviews of evaluations made by the engagement team, even though the reviewer lacks access to the same information as the engagement team;
- The standard requires the reviewer to identify risks to the performance of the engagement team, rather than to focus on risks of material misstatement of the financial statements and material weaknesses in internal control over financial reporting that the engagement team might not have identified.

In our view, the focus of an engagement quality review standard should be on *reviewing* the significant judgments made and conclusions reached by the engagement team. Our analysis and basis for our views are set forth in detail below.

Objective of the Engagement Quality Review Standard

We believe the final standard should state an objective in order to provide a clear, articulated understanding of the purpose of the standard. Having a common understanding of the overall

¹ Proposed Redrafted ISA 220, *Quality Control for an Audit of Financial Statements* (ISA 220) and Proposed Redrafted ISQC 1, *Quality Control for Firms that Perform Audits and Reviews of Financial Statements, and Other Assurance and Related Services Engagements* were proposed by the International Auditing and Assurance Standards Board in July 2007 and are scheduled to be considered for adoption by the International Auditing and Assurance Standards Board in September 2008.

purpose of the standard is important for two principal reasons. First, a statement of the objective will guide reviewers in satisfying themselves that, in doing their work, they understood and accomplished the requirements of the standard. Second, by putting the review in the proper perspective, the Board improves the likelihood that third parties -- including other regulators and the public -- will have a consistent understanding of the intent of the standard. Beyond these principal reasons for establishing an objective, we believe that doing so can also be beneficial to providing the appropriate framework for the standard-setting process itself.

We believe the objective should make clear that an engagement quality review should be just that—a review. The purpose of an engagement quality review is to provide an objective review of the engagement team’s significant auditing and accounting judgments, and the support for those judgments, by an experienced and objective colleague who, where appropriate, will question and challenge those judgments and reach a conclusion based on all relevant facts and circumstances of which he or she has knowledge. That review, properly conducted, enhances audit quality. To that end, we recommend that the Board adopt the following objective for the standard:

The objective of the engagement quality review is to provide for an independent, objective review of significant auditing, accounting, and financial reporting matters including significant judgments made and conclusions reached by the engagement team, that results in a conclusion about whether the engagement quality reviewer concurs with the issuance of an engagement report.

This language makes clear that the requirement is for a “review” of significant matters, not the performance of additional independent substantive procedures nor a complete evaluation of certain aspects of the engagement team’s work. It also serves to differentiate the function of the engagement quality reviewer from that of the engagement partner.

The engagement partner has overall and ultimate responsibility for the audit and the audit opinion. The engagement quality reviewer is an element of quality control. As such the reviewer is in the position to provide an objective review of significant auditing, accounting, and financial reporting matters, including significant judgments made and conclusions reached by the engagement team. Furthermore, the engagement quality reviewer is not, and could not as a practical matter be, responsible for the audit. Unlike the engagement team, the engagement quality reviewer's access to client records is generally limited to the audit documentation and discussion with the engagement team; he or she generally has limited, if any, interaction with client personnel.

These limitations preclude the reviewer from independently forming the necessary judgments and conclusions required throughout the audit. Therefore, the purpose of the standard should not be to create an additional level of independent substantive auditing procedures, to engage in substantive

oversight over the audit engagement team, to substantively evaluate the performance of the engagement team, or to determine compliance with the audit documentation requirements. The objective recommended above would make that clear.

We believe the Board should not adopt an objective that could be interpreted to result in an engagement quality review that mirrors or overlaps with the engagement partner's responsibilities or other quality reviews such as a firm's internal quality control program and PCAOB inspections. The other firm-wide monitoring procedures and PCAOB inspections have distinct but different purposes and are generally conducted by teams of people, subsequent to the issuance of the engagement report and without timing constraints.

The Proposed Standard

Measured against our suggested objective, we are concerned about certain aspects of the Board's proposal. First, as further described below, we believe that the proposed standard goes well beyond the requirements of international auditing standards. Second, we believe that the proposed changes and additions to what is required by the Board's current interim standard (as well as by international auditing standards) will significantly alter the nature of an engagement quality review and result in additional costs, which could be significant, without providing a commensurate benefit to audit quality. Incremental costs, in proportion to total audit fees, likely would be higher for smaller issuers than for larger issuers.

We believe that these concerns should be addressed by aligning the new standard with international standards, which we believe would create an appropriately focused and effective review standard. Moreover, doing so would be consistent with the growing demand for convergence of world-wide accounting and auditing standards and the recognition of the benefits of developing a single set of standards for world-wide use. We believe that further consideration should be given to the benefits of convergence and to avoiding the creation of unnecessary substantive differences in standards.

If, however, the Board does not believe convergence of this standard with international standards is appropriate, we urge the Board to, at minimum, consider and address the concerns about those provisions that differ significantly from international standards. We have recommended specific changes that we believe would appropriately support audit quality without the attendant costs of certain of the provisions in the Board's proposed standard. We believe that our recommended changes would result in a standard that is not only effective at meeting our proposed objective, but also one that can be implemented efficiently. We also have provided additional comments pertaining to certain other aspects of the proposed provisions in an Appendix to this letter.

More specifically and as more fully discussed below, we are concerned about the following incremental procedures in the proposal:

- A requirement that the engagement quality reviewer identify areas of “higher risk,” not of material misstatement, but rather areas where, regardless of materiality, the engagement team might have failed to obtain sufficient competent evidence or might have reached an inappropriate conclusion (paragraph 9);
- A requirement that the engagement quality reviewer independently evaluate the adequacy of audit documentation, particularly its compliance with Auditing Standard No. 3, *Audit Documentation* (paragraph 10);
- Procedures that require the engagement quality reviewer to make “evaluations” or “determinations” that, without clarification, might be interpreted to require efforts similar to those required of the engagement team in performing the work itself, rather than a review of the engagement team’s judgments and conclusions (paragraphs 7 and 8); and
- A new standard of performance for the engagement quality reviewer’s work and a conclusion that departs from the negative assurance in the interim standard and, as proposed, requires an affirmative conclusion. The proposal would require the reviewer to affirmatively conclude that there is nothing the reviewer “knows or *should know*” that would preclude concurrence in the engagement team’s issuance of the report (paragraph 12) (*italics added*).

These provisions, taken together, would impose substantial new burdens on the engagement quality reviewer without a commensurate benefit to audit quality. As discussed above, the objective of the review should be to enhance audit quality by providing an independent, objective review of the significant accounting and auditing judgments and the conclusions reached. The proposed standard, however, would redirect the focus of the engagement quality reviewer away from the work of the engagement team to the work performed to carry out the reviewer’s responsibilities. More specifically, in creating new standards of performance for the reviewer that require a “know or should know” level of assurance, these provisions become too focused on the adequacy of the engagement quality review itself, rather than on the quality of the work performed by the engagement team. For example, we believe that an engagement quality reviewer likely would interpret these provisions as a requirement for him or her to perform sufficient work to have a basis for separately forming his or her own independent determinations about such matters as whether appropriate consultations have taken place, whether appropriate matters have been communicated to the audit committee, whether there are areas that create a “higher risk” of non-compliance, and whether the engagement team complied with documentation standards.

Of course, issues should be raised by a reviewer if they are identified during the course of the procedures performed. However, by mandating separate determinations and judgments to be made

by the reviewer, the focus of the proposed standard is the reviewer's own basis for the determinations he or she makes in the engagement quality review, rather than the reviewer's consideration of the judgments and conclusions reached by the engagement team in the audit. The judgments the reviewer makes will likely be seen as wholly separate from, rather than enhancing or confirming, those of the engagement team.

We believe firms, clients, and investors should continue to expect engagement partners to make reasonable judgments. Engagement quality reviews, along with the other quality control processes, combine to provide a firm with reasonable assurance about the effectiveness of its system of quality control, as is required. However, we see neither a purpose nor benefit in the redirection of focus of the engagement quality review or from the additional costs that will undoubtedly be incurred.

Our concerns are compounded by the new "know or should know" standard that changes the basis upon which the reviewer can concur in the issuance of the report. Under the current interim standard, the reviewer could concur so long as "no matters have come to his or her attention that would cause the [reviewer] to believe" that the financial statements did not conform to GAAP in all material respects or that the audit was not performed in accordance with GAAS. This is a "negative assurance" standard. The proposed standard, in effect, requires the reviewer, like the engagement partner, to determine that he or she has sufficient grounds to positively concur with the issuance of the report. It converts the engagement quality reviewer's conclusion to one that requires an affirmative finding or representation that, by definition, must be based on the performance of sufficient procedures to support the finding or representation.

We have a number of concerns about the proposed change in approach to an engagement quality review. First, the requirement that the reviewer make a positive determination about whether the report should be issued is directly contrary to the objective of the review; it comes far too close to, or could even be said to replicate, the judgment made by the engagement partner. Second, because of the limitations on what a reviewer can do without impairing objectivity, the reviewer's conclusion by extension will be based on limited information. The information gap between what the engagement partner knows and the engagement quality reviewer knows, will necessarily -- but we suggest inappropriately -- raise the question about what the reviewer *should have known*. Third, the introduction of a "should know" standard would be likely to have unintended consequences given the focus it brings to the potential for being second-guessed, particularly in the absence of an objective standard or specific direction about what is required to comply. It is reasonable to assume that many reviewers will interpret the required procedures in such a way that results in significant additional work for the purpose of anticipating a defense to any subsequent challenge.

We do not believe that imposing these kinds of requirements directly on the engagement quality reviewer will result in commensurate benefit to audit quality. We believe that a reviewer, who

conscientiously performs the procedures outlined in paragraph 8, as amended by our proposed revisions below, will appropriately contribute to audit quality by focusing on the significant matters addressed by the engagement team and providing an independent review of the engagement team's judgments and support for those judgments.

In addition to the aforementioned concerns, based on discussions with various smaller member firms, we are concerned that the "should know" concept in the standard will result in a general inability for firms that need to engage a third-party engagement quality reviewer to find individuals willing to accept such a review engagement. A consequence to some smaller firms that seek to engage such a third-party engagement quality reviewer likely would be either to assign a less-qualified manager or director to perform the review or to conclude that they can no longer serve issuer clients.

The following sections explain in more detail our concerns with the particular sections of the standard and set forth our recommended changes to the Board's proposal to address our concerns. We believe that our recommended changes are consistent with the objective we proposed.

Scope of Review

Paragraphs 7 and 8 prescribe general standards and specific procedures for conducting the engagement quality review. We generally agree with the nature of these procedures to be performed. However, we recommend a change to paragraph 7 and certain changes in the text of paragraph 8 (set forth below) to clarify what procedures will satisfy the reviewer's responsibility to make the requisite evaluation and to avoid any suggestion that the reviewer is required -- or indeed able -- to duplicate the work of the engagement team or to make independent judgments about matters that are the responsibility of the engagement team.

These recommended changes, included herein, would make the expected level of work more clear and avoid a fundamental change in the nature of the review function, which could otherwise potentially compromise the important principles of objectivity underlying the standard. The standard, we believe, should reinforce, not diffuse, the accountability of the engagement partner.

Based on the foregoing, we recommend that the Board consider revising paragraphs 7 and 8 of the proposed standard. In addition to changes to implement our comments above, we believe certain provisions in paragraph 8 should be clarified to provide more certainty about how to satisfy the presumptively mandatory requirements in each of these sections:

7. The engagement quality reviewer should evaluate ~~include an evaluation of the significant judgments made by the engagement team and the significant conclusions reached by the engagement team in forming the overall conclusion on in conducting~~

the engagement and in preparing the engagement report, if a report is to be issued. ~~To identify and evaluate the significant judgments and conclusions,~~ The evaluation should be conducted by the engagement quality reviewer should include through discussions with the person with overall responsibility for the engagement, discussions with other members of the engagement team as necessary appropriate, and other procedures, as described in paragraphs 8 and 9.

8. As part of performing the engagement quality review, the engagement quality reviewer should:

- a. ~~Obtain an understanding of the firm's recent engagement experience with the company and risks identified in connection with the firm's client acceptance and retention process~~ for the company.
- b. Obtain an understanding of the company's business, significant activities during the current year, and significant financial reporting issues and risks through discussions with the person with overall responsibility for the engagement, discussions with other members of the engagement team, as appropriate, and the performance of the procedures enumerated in the subparagraphs below.
- c. Review the engagement team's evaluation of the firm's independence in relation to the engagement (i.e., the communication with the audit committee required by Rule 3526, *Communication with Audit Committees Concerning Independence*, formerly Independence Standards Board Standard No. 1, *Independence Discussions with Audit Committees*).
- d. ~~Evaluate~~ Review engagement planning, including (1) the judgments made about materiality and the effect of those judgments on the engagement strategy and (2) the identification of significant risks of material misstatement to the financial statements and the risks of material weakness in internal control over financial reporting, including fraud risks, and the plan for and performance of engagement procedures in response to those risks.
- e. ~~Evaluate~~ Review judgments made about (1) the materiality and disposition of corrected and uncorrected identified misstatements and (2) the severity and disposition of identified control deficiencies.
- f. ~~Determine if appropriate consultations have taken place on difficult or contentious matters.~~ Review the documentation, including conclusions, of such consultations that have taken place on significant difficult or contentious matters.



- g. Read the financial statements, management's report on internal control over financial reporting, or other information that is the subject of the engagement and the engagement report (if an engagement report is to be issued) for the period covered by the engagement and for the prior comparative periods presented.**
- h. Read other information in periodic filings and offering documents, as applicable, containing financial statements that are the subject of the engagement and are to be filed with the SEC and evaluate whether the engagement team has taken appropriate action with respect to material inconsistencies with the financial statements or material misstatements of fact of which the engagement quality reviewer is aware.**
- i. ~~Determine if~~ Review whether appropriate matters of which the engagement quality reviewer is aware have been communicated, or identified for communication to the audit committee, management, and other parties, such as regulatory bodies.**
- j. Review the engagement completion document and confirm with the person with overall responsibility for the engagement that there are no significant unresolved matters.**

Note: Matters of which the engagement reviewer is “aware” are those matters that have come to the attention of the reviewer during the course of performing the procedures required by this standard.

Engagement Quality Reviewer Risk Assessment

Paragraph 9 of the proposed standard requires the reviewer to identify areas within the engagement that pose a “higher risk.” The term “higher risk” in that paragraph is not, however, directed to the potential for material misstatements or any other objective standard. Rather, the standard focuses on the “higher risk” that the engagement team failed to obtain sufficient competent evidence or reached an inappropriate conclusion. For the areas that pose such “higher risk,” the engagement quality reviewer is required to evaluate whether the engagement team performed procedures that were responsive to those risks, whether the judgments made by the engagement team were reasonable in the circumstances, and whether the results of the procedures support the engagement team’s overall conclusion.

We believe it is important that the engagement quality reviewer understand and review the significant risks of material misstatement to the financial statements and the risks of material weakness in internal control over financial reporting identified by the engagement team and the

engagement team's response to such risks. We do not believe that requiring a separate assessment of the risk that the engagement team failed to obtain sufficient competent evidence or reached an inappropriate conclusion is workable or consistent with the objective of an engagement quality review.

First, we question how the engagement quality reviewer would make such a determination. For example, what considerations would be deemed sufficient to support this determination, particularly without the benefit of the information available in hindsight when his or her review is scrutinized? The standard does not articulate any procedures for making this determination, other than referring to the procedures in paragraphs 7 and 8 and "other relevant knowledge possessed by the engagement quality reviewer." Second, we note the Board's use of the term "higher risk." Being a relative term, it implies that there should always be some areas of higher risk, even though there might be no audit areas that pose a sufficiently high risk to justify further consideration or action. Third, we believe this requirement to be more concerned with having the reviewer make risk assessments separate from the engagement team, rather than reviewing the engagement team's own judgments for reasonableness. We question the focus of this requirement and the extent to which it will result in improvement to audit quality. Finally, we note that paragraph 12, both as proposed and consistent with our recommended revision, already contains a sufficient provision to prevent engagement quality reviewers from concurring with the issuance of the engagement report if, based upon the engagement quality review procedures performed, the reviewer believes that the engagement team failed to obtain sufficient competent evidence in accordance with PCAOB standards or reached an inappropriate conclusion about the subject matter of the engagement.

We recommend that the Board modify the proposed requirement in paragraph 9 to refocus it on whether important matters were identified during the engagement quality review that were not previously identified by the engagement team. Those matters should include the significant risks of material misstatement to the financial statements, significant risks of material weakness in internal control over financial reporting, and significant difficult or contentious matters that the engagement team might not have identified where consultation by the engagement team should be considered. If such matters are determined to exist, the engagement quality reviewer should be required to communicate these matters to the engagement team and assess whether the engagement team responds or has responded appropriately.

As such, we recommend that paragraph 9 be revised to read as follows:

9. Based on the procedures performed in accordance with paragraphs 7 and 8, and the engagement quality reviewer's knowledge, the engagement quality reviewer should assess whether any of the following matters were not previously identified by the engagement team:

- significant risks of material misstatement to the financial statements,
- significant risks of material weakness in internal control over financial reporting, or
- significant difficult or contentious matters where consultation should be considered by the engagement team.

If the engagement quality reviewer believes that there are such risks or matters, he or she should communicate that to the engagement team and then assess whether the engagement team has responded appropriately.

Review of Engagement Documentation

Paragraph 10 of the proposed standard would require the engagement quality reviewer to evaluate the engagement documentation. In particular, it requires the reviewer to evaluate whether the documentation “is appropriate in the circumstances and consistent” with the Board’s Auditing Standard No. 3, *Audit Documentation* (AS 3).

We believe audit documentation is important and we support the Board’s proposed requirement for an engagement quality reviewer to assess whether the engagement documentation supports the conclusions reached by the engagement team with respect to the matters reviewed by the engagement quality reviewer. However, we believe that the proposed standard, if not modified, could impose substantial additional burdens on the engagement quality reviewer to review the adequacy of documentation rather than the appropriateness of the significant accounting and auditing judgments made by the engagement team, and that result would not meaningfully enhance audit quality. We therefore recommend that the standard be modified in the following respects.

First, we believe the requirement to evaluate documentation should be limited to assessing that which is reviewed in connection with the procedures required by paragraphs 7 - 9 of the proposed standard. Absent such a limitation, the proposed standard might be interpreted to extend the engagement quality reviewer’s responsibilities to require him or her to conduct a separate review of all or much of the engagement documentation.

Second, we believe that the final standard should omit the requirement that the engagement quality reviewer evaluate whether the audit documentation is consistent with AS 3. We do not believe that this specific requirement is consistent with the overall objective of the engagement quality review, nor do we think it will meaningfully enhance audit quality. The engagement partner has primary responsibility for performance of the audit, including performing a review of the documentation for compliance with AS 3. It is not, and should not be, the engagement quality reviewer’s responsibility to duplicate that evaluation. Furthermore, we do not believe it is appropriate or necessary to single out any particular auditing standard for this type of compliance check by the reviewer.

We believe requirements in paragraphs 9 and 10 of the proposed standard potentially duplicate other requirements of AS 3. In addition, paragraph 13 of AS 3 requires that the engagement team “identify all significant findings or issues in an engagement completion document.” Paragraph 13 further states that “this document, along with any documents cross-referenced, should collectively be as specific as necessary in the circumstances for a reviewer to gain a thorough understanding of the significant findings or issues.” In our view, a qualified engagement quality reviewer should be able to achieve the objectives for the engagement quality review by performing the procedures outlined in paragraphs 7 and 8 of the proposed standard, as amended by our proposed revisions above, which reflect existing requirements and would include reviewing the engagement completion document.

Third, we recommend that the Board revise paragraph 10 to make it clear that the scope of the engagement quality review is to assess whether the documentation that the reviewer selected for review supports the conclusions that were reached by the engagement team. That assessment will include considering significant risks of material misstatement to the financial statements and the risks of material weakness in internal control over financial reporting and significant judgments by the audit team. Our recommended change, however, eliminates an implication that paragraph 10 creates a more general requirement to assess matters that are not encompassed by the procedures set forth in paragraphs 7 - 9.

Accordingly, we recommend that paragraph 10 of the proposed standard should be revised to read as follows:

10. Engagement Documentation. Based upon the procedures performed in accordance with paragraphs 7, 8, and 9, the reviewer should assess whether the engagement documentation reviewed during the course of the engagement quality review supports the significant conclusions reached by the engagement team.

Concurring Approval of Issuance

Paragraph 12 of the proposed standard provides that the engagement quality reviewer cannot provide “concurring approval” of the issuance of an engagement report if he or she “knows or should know” that any of four enumerated conditions exist.

We believe that the engagement quality reviewer’s concurrence is an important contribution to audit quality. We agree with the Board’s enumeration of the four conditions that, if present, would preclude the engagement quality reviewer from concurring with the issuance of the engagement report. We also support the requirement that the engagement quality reviewer consider the knowledge obtained in performing the review in accordance with the standard. However, we believe that the inclusion of the legalistic “knows or should know” formulation for approval in auditing

standards is neither necessary nor appropriate. The terminology would likely lead to misunderstanding and inconsistent application of the standard. For example, referring to what the reviewer “knows, or should know based upon the requirements of this standard” implies that the reviewer must perform sufficient procedures under the requirements of the standard to “know” that the four specified conditions do not exist. This would likely lead engagement quality reviewers to engage in substantial procedures to conclude that they do not know that any of the specified conditions are present. The term “should know” is even more troubling. It inherently creates a potential for post-hoc questioning of whether an engagement quality reviewer should have identified a condition that would have precluded him or her from concurring in the issuance of the engagement report. Accordingly, we believe that engagement quality reviewers will be overly focused on being second-guessed as to what they should have known, if a problem with the audit is later identified, rather than on assisting the engagement team by reviewing significant judgments and conclusions.

As a result, the engagement quality reviewer would likely spend substantially more time, perform substantially more procedures and incur more costs than the reviewer would otherwise consider necessary, or we believe appropriate, in connection with a review. We strongly believe that the cost-effective improvement to audit quality should be the primary objective. We do not believe that inclusion of a “know or should know” standard of performance for the engagement quality reviewer furthers that objective. We recommend that paragraph 12 of the proposed standard be revised to remove the words “knows, or should know” by either conforming to the language used in ISA 220², or alternatively, as follows:

12. The engagement quality reviewer must not ~~provide concurring approval of~~ concur with the issuance of an engagement report if, ~~he or she knows, or should know based upon his or her review in accordance with the requirements of this standard,~~ the reviewer believes that (1) the engagement team failed to obtain sufficient competent evidence in accordance with the standards of the PCAOB, (2) the engagement team reached an inappropriate overall conclusion on the subject matter of the engagement, (3) the firm's report, if a report is to be issued, is not appropriate in the circumstances, or (4) the firm is not independent of its client.

We believe that the proposed language retains the essence of the standard—that the reviewer cannot concur if he or she believes, based on the review, that any of the four enumerated conditions are present. However, it eliminates the inappropriate “knows or should know” standard.

² Paragraph 22(c) of Proposed and Redrafted ISA 220 requires the reviewer to document that “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.”

Effective Date

As proposed, the standard would be effective for reports issued on or after December 15, 2008. We are concerned that the proposed effective date would not permit sufficient time for registered public accounting firms to implement the new engagement quality review requirements. The effective date should provide all registered public accounting firms with sufficient time to (1) adopt policies and procedures consistent with the new standard, (2) train their personnel in the requirements of the new standard, and (3) assign qualified engagement quality reviewers consistent with their system of quality control.

We also believe that the effective date should be linked to the beginning of an engagement period. By linking the effective date to the beginning of the engagement period rather than the report issuance date, the new requirements would (1) be known and anticipated as of the beginning of the engagement period, (2) allow the assigned engagement quality reviewer to comply with the requirements throughout engagement planning and execution, and (3) be in place for each quarterly review conducted under AU section 722, *Interim Financial Information*.³ In this manner, adoption of the new standard would be more effective and efficient.

To the extent that the new standard contains more extensive requirements than the Board's interim standard, the PCAOB should delay the effective date to annual periods beginning no earlier than twelve months after SEC approval to provide adequate time for firms to prepare for adoption.

Potential Effect on Ability to Complete Review Timely

In the event that the Board does not make significant modifications to the proposed standard to address the matters raised in our comment letter, we question whether some issuers and auditors would be able to meet the SEC's accelerated filing deadlines, given the fact that a significant portion of engagement quality review work must be performed near the end of the engagement. Accordingly, absent significant modifications, we recommend that the PCAOB discuss with the SEC, the effect of the standard on issuers' ability to meet SEC filing deadlines and whether such deadlines would need to be modified.

* * * * *

We appreciate the opportunity to comment on the proposed standard and would welcome the opportunity to meet with you to discuss any of our comments.

³ Our concerns regarding the requirements of the proposed standard relative to reviews of interim financial information are included in the Appendix to this letter under "Scope of Proposed Standard."

Sincerely,



Cynthia M. Fornelli
Executive Director
Center for Audit Quality

Cc: PCAOB
Mark W. Olson, Chairman
Daniel L. Goelzer, Member
Willis D. Gradison, Member
Charles D. Niemeier, Member
Thomas Ray, Chief Auditor and Director of Professional Standards

SEC
Chairman Christopher Cox
Commissioner Paul S. Atkins
Commissioner Kathleen L. Casey
Conrad Hewitt, Chief Accountant
Dr. Zoe-Vonna Palmrose, Deputy Chief Accountant for Professional Practice
John W. White, Director of Division of Corporation Finance



Appendix

Set forth below are additional comments pertaining to certain other aspects of the proposed standard.

Scope of Proposed Standard

While we acknowledge the Board's desire for the engagement quality review standard to apply to all engagements performed in accordance with the standards of the PCAOB, the requirements in the proposed standard are so specifically tailored to financial statement audits and integrated audits that it would be difficult to apply certain requirements to other types of engagements with appropriate consistency. For some engagements, it might be appropriate to presume that certain requirements do not apply (for example, reading management's report on internal control would not apply in a review of interim financial statements). However, in other situations, the Board's intent is less clear. For example:

- Would the engagement quality reviewer be expected to obtain an understanding of significant financial reporting issues and risks (paragraph 8(b)) when reviewing an attestation engagement on the assessment of compliance with servicing criteria under the SEC's Regulation AB?
- What is the "prior period" (paragraph 8(g)) in the case of a third-quarter review of interim financial information?

Furthermore, with respect to the evidence required to be assessed ("sufficient competent evidence"), and the nature of the affirmative conclusion, the proposed standard appears to place the engagement quality reviewer in a position of having to obtain more evidence and, consequently, to provide a higher level of assurance than the engagement team for certain engagements – for example, a review of interim financial information or a comfort letter for underwriters.

More specifically regarding a review of interim financial information, we are concerned that the requirements of the proposed standard are not consistent with the objective of a review of interim financial information. The objective of a review of interim financial information is "to provide the accountant with a basis for communicating whether he or she is aware of any material modifications that should be made to the interim financial information for it to conform with generally accepted accounting principles."⁴ Toward that objective, a review consists principally of analytical procedures and inquiries of management. Some examples of what we believe to be inconsistencies between the requirements of the proposed standard and a review of interim financial information follow:

⁴ AU 722.07



- Paragraphs 8d and 10 of the proposed standard include requirements for the engagement quality reviewer to evaluate the engagement team's identification of, and responses to, significant risks. While a review of interim financial information involves assessment of risk in designing appropriate analytical and inquiry procedures, the terminology used in the proposed standard relates to an audit engagement, and we ordinarily would not expect an engagement team's documentation in a review of interim financial information to include explicit risk assessments. Accordingly, the Board's expectation of the engagement quality reviewer concerning risk assessment in a review of interim financial information is unclear.
- Paragraph 9 would require the engagement quality reviewer to assess whether there are areas within the engagement that pose a higher risk that the engagement team failed to obtain sufficient competent evidence or to reach an appropriate conclusion. As obtaining sufficient competent evidence is not a part of a review of interim financial information, we believe paragraph 9 will result in confusion and inconsistent practice in a review of interim financial information, notwithstanding the phrase "or to reach an appropriate conclusion." Paragraph 12 also refers to sufficient competent evidence
- Paragraph 12, as proposed, requires the engagement quality reviewer to provide an affirmative conclusion. Given that the objective of a review of interim financial information is to provide negative assurance, we do not believe it is appropriate for the engagement quality reviewer to reach a conclusion that is different than and goes beyond that which is required of the engagement team.

The Board therefore should identify the engagement quality review procedures required for interim reviews, provide clarity regarding the applicability of the procedures, and modify the conclusion to be reached by the engagement quality reviewer in connection with interim reviews. Specifically, the Board should include in the final standard an additional section, analogous to paragraph 7, that requires the engagement quality reviewer, in a review of interim financial information, to "discuss significant matters identified and addressed in connection with the review." Similarly, the final standard should require that only a subset of procedures set forth in paragraph 8 (specifically those set forth in subparagraphs 8(g), 8(h), 8(i), and 8(j), as revised pursuant to the suggestions herein) be completed for interim reviews. Finally, the final standard should clarify that the engagement quality reviewer is required to provide only negative assurance of concurring approval in the context of an interim review, consistent with the overall conclusion of such a review.⁵

We also recommend that the Board reconsider the practicality of applying the proposed standard to engagements other than financial statement audits, integrated audits, and reviews of interim financial information. If the Board believes engagement quality reviews are desirable for such engagements,

⁵ Our concerns regarding the proposed requirement for an affirmative conclusion by the engagement quality reviewer in an audit engagement are included in this letter under "Concurring Approval of Issuance."

we believe that the Board should develop a separate standard that allow the procedures to be tailored appropriately to the engagement circumstances. For example, we believe that a requirement to apply an auditing standard to an engagement performed in accordance with attestation standards would result in confusion and inconsistent practice. Accordingly, we believe any engagement quality review requirement for attestation engagements should be provided for in the attestation standards rather than the auditing standards.

Qualifications of the Engagement Quality Reviewer

Competence

The proposed standard, in paragraph 2, indicates that the engagement quality reviewer may be a partner in the engagement partner's firm or another individual in the firm (or an individual outside the firm). Paragraph 4 of the proposed standard then states that "the engagement quality reviewer must possess the level of knowledge and competence related to accounting, auditing, and financial or other reporting required to serve as the person who has overall responsibility for the same type of engagement." While these statements are not necessarily contradictory, considered together, they are confusing. For example, one could argue that a senior manager cannot meet the definition of "competent," as a senior manager could not, by virtue of his or her title, be an engagement partner who has "*overall responsibility for the same type of engagement.*" Similarly, a person outside of the firm would have the same issue. We recommend that the Board reemphasize for clarity, in paragraph 4, that the engagement quality reviewer need not be a partner, notwithstanding the requirement to "possess the level of knowledge and competence related to accounting, auditing, and financial or other reporting required to serve" as the engagement partner.

Page 9 of the proposing release provides, as an example of the appropriate knowledge and competence of an engagement quality reviewer, a statement that a person assigned to perform the engagement quality review for an audit of a company involved in "oil and gas exploration" should have experience sufficient to serve as the engagement partner in this specialized industry. We are concerned that this example places too much focus on specialized industry expertise and again suggests that the engagement quality reviewer in all instances should be a partner. We recommend removing this example from the release, and including a statement in paragraph 4 of the standard that "considerations in evaluating competence include, but are not limited to, technical expertise, experience, knowledge of SEC rules and regulations pertinent to the engagement, and industry knowledge."

Footnote 18 of the Board's proposing release states, "The determination of what constitutes the appropriate level of knowledge and competence should be based on the circumstances of the engagement, including the size or complexity of the business." We believe this statement is useful guidance and reflects the concept of judgment necessary when assigning an engagement quality reviewer to an engagement, and we recommend that it be added to the standard.

Independence, Integrity, and Objectivity

We are concerned that the language in paragraphs 5 and 6 of the proposed standard redefines the notion of objectivity as it is currently explained in the PCAOB professional standards, and that this language, which is written very broadly, might be misinterpreted in a way that could negatively affect audit quality. Our specific comments regarding objectivity as it relates to communication between the engagement quality reviewer and the engagement team and communication between the engagement quality reviewer and the audit committee or management are set forth below.

Communication between the Engagement Quality Reviewer and the Engagement Team

Paragraph 5 of the proposed standard explains that “The engagement quality reviewer must be independent of the company, perform the engagement quality review with integrity and maintain objectivity with respect to the engagement and the engagement team” (emphasis added). While we agree the engagement quality reviewer must maintain objectivity, paragraph 5 could be interpreted to suggest that the Board is changing the definition of the word “objectivity.” Historically, “objectivity” has been defined with respect to the audit; that is, the engagement team and the concurring review partner are required to perform their procedures with skepticism and objectivity.

Furthermore, the note to paragraph 6 of the proposed standard and footnote 19 of the proposing release also could be interpreted to limit the discussions between the engagement team and the engagement quality reviewer. The note to paragraph 6 states the following: “The engagement team may consult with the engagement quality reviewer on matters during the course of the engagement. When participating in such consultations, the engagement quality reviewer should not participate in a manner that would compromise his or her objectivity with regard to the engagement” (emphasis added). We believe that consultation is an important element of audit quality and that the standard should encourage consultation with the engagement quality reviewer.

To avoid the unintended consequence of limiting communications between the engagement team and the engagement quality reviewer that we do not believe compromise objectivity, we recommend:

- Replacing the language in paragraph 5 with language similar to that of QC Section 20, so that it states the following: “Engagement quality reviewers must be independent of the company and perform all professional responsibilities with integrity, and maintain objectivity in discharging professional responsibilities.”⁶

⁶ See PCAOB Interim Standards, QC 20.09.

- Removing the second sentence of the note to paragraph 6. If the Board is concerned about the engagement quality review partner making an objective assessment, the standard could include language similar to that in the Board's interim standard on concurring reviews as follows:

“When discussion occurs with the concurring partner reviewer on an accounting, auditing, or financial reporting matter during the engagement, the audit engagement partner ordinarily should develop an initial resolution to the matter before discussion with the concurring partner reviewer.”

We note this language appears on page 11 of the Board's proposing release. Incorporating this language in the standard will make it clear that the Board is not intending to limit communications between the engagement quality reviewer and the engagement team or change the manner in which the two interact.

Communications between the Engagement Quality Reviewer and the Audit Committee or Management

We note that the standard is silent with respect to appropriate communications between the engagement quality reviewer and the audit committee or management. Without guidance on this topic, the proposed standard could be read to discourage such communications.

To address this concern, we recommend that the standard include guidance that communications between the engagement quality reviewer and management or the audit committee would not necessarily compromise objectivity. In addition, we recommend that the standard adopt the language that is in footnote 3 of the PCAOB's interim standard on concurring reviews: “A client may contact the concurring partner reviewer with respect to matters requiring immediate attention when the audit engagement partner is not available because of illness, extended travel or other reasons. When a concurring partner reviewer is thus required to deal with an accounting, auditing or financial reporting matter, he or she should advise the audit engagement partner of the facts and circumstances so that the audit engagement partner can review the matter and take full responsibility for its resolution.”

Documentation of an Engagement Quality Review

Paragraph 14 of the proposed standard, regarding documentation of an engagement quality review, is unclear in some respects and could lead to significant divergence in practice. To add clarity, we recommend that the Board consider including a requirement consistent with paragraph 27 of the International Auditing and Assurance Standards Board's Proposed Redrafted International Standard on Auditing (“ISA”) 220, *Quality Control for an Audit of Financial Statements*, which states:

The engagement quality control reviewer shall document, for the audit engagement reviewed, 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 date of the auditor's report; 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.⁷

In case the Board decides to retain documentation requirements along the lines of paragraph 14 of the proposed standard, we are concerned specifically that the Board's intent in paragraphs 14(b), (d), and (e) is unclear as described in the following paragraphs.

Paragraph 14(b) requires that the areas of the engagement subject to the engagement quality review be documented. In our view, an entire engagement is subject to the engagement quality review. However, if that interpretation is what the Board intended, it would not seem necessary to document that the engagement was subject to an engagement quality review, as that point would be self-evident from the engagement quality reviewer's concurring approval of issuance of the auditor's report. If the Board's intention is for the documentation to reflect which individual work papers were reviewed or something else, we recommend that the Board clarify that point.

Paragraph 14(d) requires that the engagement documentation reflect "when the review procedures were performed." An engagement quality review involves a variety of procedures, including review of individual work papers, review of draft financial statements and SEC filings, and discussion with the engagement partner and other engagement team members. If the Board's intent is that the engagement quality reviewer document when he or she reviews individual work papers, we recommend that this point be clarified. We do not believe, however, that it is appropriate for there to be a higher standard for documentation for engagement quality reviewers than for members of the engagement team or that such a standard would provide a benefit commensurate with the significant effort.

Paragraph 14(e) requires that the results of the review procedures be documented. We believe some auditors may view "the results of the review procedures" to be whether issuance of the auditor's report is approved. If this interpretation is correct, this requirement is redundant with paragraph 14(f), which requires documentation of whether the engagement quality reviewer provided concurring approval of issuance. We believe others may view "the results of the review procedures" to denote a detailed record of considerations made by the engagement quality reviewer, questions asked of the engagement team (e.g., review notes) with documentation of the engagement team's

⁷ Our concerns regarding the proposed requirement for an affirmative conclusion by the engagement quality reviewer in an audit engagement are included in this letter under "Concurring Approval of Issuance."



responses, etc. The latter interpretation would result in an effort substantially incremental to practice under the Board's interim standard and the need for a significant increase in engagement quality reviewer resources, with minimal benefit. We recommend that the Board eliminate paragraph 14(e) to avoid confusion and unnecessary effort.



May 2, 2008

Office of the Secretary
PCAOB
1666 K Street, N.W.
Washington, DC 20006-2803

RE: PCAOB Rulemaking Docket Matter No. 025

Dear Mr. Scates, Ms. Campbell, PCAOB Board Members and Staff:

Thank you for the opportunity to comment on the Board's Proposed Auditing Standard, "Engagement Quality Review." On balance, I think this is an excellent proposed standard. I will briefly highlight what I view as the strengths of the proposal, and make a few limited suggestions as to how the proposed standard might be improved.

The proposed standard has three noteworthy features. First, the proposed standard requires that an engagement quality review be performed on all engagements performed under the standards of the PCAOB. Currently, engagement quality reviews are only performed for audits performed by SECPS member firms as of 2003. In addition to requiring engagement quality reviews for audits performed by registered firms that were not members of the SECPS (presumably a limited number), the proposed standard would require that an engagement quality review be performed for all auditor reviews of quarterly information filed on a Form 10-Q. The academic literature documents that quarterly information is relevant to the capital markets and that quarterly financial information is generally less reliable. Therefore, efforts by the Board to increase the quality of quarterly reviews performed by auditors will benefit the investing public. Requiring an engagement quality review on quarterly reviews performed by the auditor should increase the quality of this work. Second, the proposed standard is informed by PCAOB inspection findings and by recent PCAOB enforcement cases. Unlike other standard setters, the PCAOB can tailor standards to address deficiencies identified during inspections and enforcement cases. Third, prohibiting the firm from issuing the report until the engagement quality reviewer gives his or her concurrence provides the quality reviewer with leverage if he or she disagrees with the engagement partner.

I believe that the proposed standard could be improved in three ways. First, I believe the proposed standard should state an overall objective for the engagement quality review. In

my view, the overall objective of the proposed standard should be, “The engagement quality reviewer is to perform the review to evaluate whether the engagement has been planned and performed to provide reasonable assurance that material misstatements will be detected, whether caused by error or fraud.”¹ This is what financial statement users care about. Second, the firm should be required to document its conclusion as to why the quality reviewer has the qualifications needed “... to serve as the person who has overall responsibility for the same type of engagement.” This is particularly important where someone other than another partner from the firm performs the review (e.g., a non-partner employee of the firm, a partner from another registered firm, an outside consultant, etc.). Moreover, to continue to build important feedback loops between different PCAOB divisions, the firm’s evaluation of the qualifications of the engagement quality reviewer should be carefully evaluated by the PCAOB’s inspection staff, especially in the early years that this standard is effective. Third, the engagement quality reviewer (to the extent practicable) should not be included in the same office-level profit pool as the engagement partner. For example, if Firm ABC audits Company XYZ out of the Atlanta office and if Firm ABC partially compensates partners based on local-office profitability, the engagement partner should not be from the Atlanta office.²

In my view, the proposed standard, Engagement Quality Review, has the potential to improve audit practice. I encourage the Board to move expeditiously to approve it.

Sincerely,

Joseph V. Carcello
Ernst & Young Professor
Director of Research – Corporate Governance Center

¹ This proposed objective applies to engagement quality reviews of audit engagements. Appropriately-modified language could be developed for engagement reviews of quarterly auditor reviews and attest engagements.

² This recommendation obviously would not apply to single-office firms, but it may be efficacious for audits performed by the largest six firms and these firms audit companies comprise the overwhelming majority of U.S. stock market capitalization.



Comcast Corporation
One Comcast Center
Philadelphia, PA 19103-2838

May 12, 2008

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

**RE: Request for Public Comment on PCAOB's Proposed Auditing Standard –
*Engagement Quality Review and Conforming Amendment to the Board's Interim
Quality Control Standards*; PCAOB Rulemaking Docket Matter No. 025**

Dear Office of the Secretary:

Comcast Corporation appreciates the opportunity to comment on the Public Company Accounting Oversight Board's (the "Board" or "PCAOB") Proposed Auditing Standard – *Engagement Quality Review* ("proposed auditing standard"). We are the largest cable operator in the United States and offer a variety of entertainment and communications products and services.

We strongly support auditing standards that promote audit quality and believe that an engagement quality review that focuses on significant judgments made and conclusions reached by the engagement team is critical to the audit process. However, we are concerned that the proposed auditing standard goes beyond what is currently needed.

Specifically our concerns are directed to the aspects of the engagement quality review standard that will likely require significant incremental procedures, which may result in additional audit fees and could lead to reporting delays.

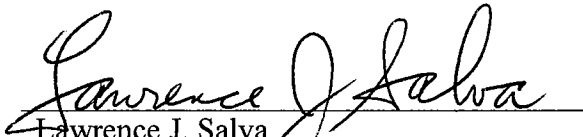
Paragraph 9 of the proposed auditing standard appears to require the quality reviewer to obtain a broader independent understanding of the audit risks of the engagement (by reference to paragraph 8.b.) and assess whether the engagement team has failed to obtain appropriate evidence or reached inappropriate conclusions in the identified risk areas. We are concerned that this will result in concurring partners believing it is necessary to repeat a large amount of the review work of the engagement partner, resulting in unnecessary costs and perhaps a delay in finalizing year end audits. We are also concerned that the "should know" standard in paragraph 12 will cause concurring partners to be concerned that PCAOB inspectors may find fault with the more limited work of a concurring partner because they think he or she should have looked at areas they found to be deficient through the comprehensive PCAOB inspection.

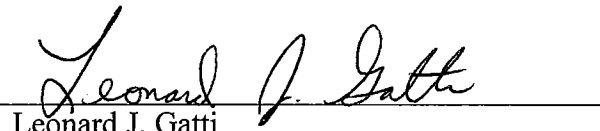
Office of the Secretary
Public Company Accounting Oversight Board
May 12, 2008
Page 2

We believe the best way to address these problems would be to simply eliminate the broad requirements of paragraph 9 and eliminate from paragraph 12 the phrase “or should know based upon the requirements of this standard.” However, we believe these problems should also be addressed by clearly stating the objective of the concurring partner review. The present draft of the standard does not specify what is supposed to be accomplished by such review and that seems like an important omission in the current “objectives-based standards” world.

We appreciate the opportunity to express our views on this proposed auditing standard.

Sincerely,


Lawrence J. Salva
Senior Vice President,
Chief Accounting Officer and Controller


Leonard J. Gatti
Vice President, Financial Reporting



May 12, 2008

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

PCAOB Rulemaking Docket Matter No. 025

Dear Secretary:

Community Health Systems (“CHS” or the “Company”) is pleased to respond to the request for comment from the Public Company Accounting Oversight Board (the “PCAOB” or the “Board”) regarding Release No. 2008-002; *Proposed Auditing Standard - Engagement Quality Review and Conforming Amendment to the Board’s Interim Quality Control Standards*, PCAOB Rulemaking Docket Matter No. 025 (the “Release”).

While we support improvement of audit quality, we are concerned that the proposed standard increases the scope of the engagement quality review without a commensurate improvement in audit quality. We understand that the PCAOB has considered information on this topic from PCAOB inspections and enforcement cases when formulating the proposed standard as well as other standards in this area.

Under the existing requirements, the concurring partner is required to review those significant auditing, accounting and financial reporting matters, discuss the engagement team’s identification and audit of high-risk transactions and balances, review documentation on the resolution of significant accounting, auditing and financial reporting matters, review the summary of unadjusted audit differences, read the financial statements and auditor’s report, and confirm with the engagement partner that there are no significant unresolved matters. This concurring partner review is required to be completed before the audit report is released.

The Release indicates that some members of the Board’s Standing Advisory Group believe that the existing requirements “did not provide for a thorough review to achieve the objectives of the requirement and that the reviews generally need to be more robust to provide investors with assurance on the quality of audit engagements.” Please consider the following:

- We believe the concurring review process currently used by our audit firm is sufficiently robust post-Sarbanes Oxley and question whether the additional engagement quality review requirements would add value. We are also concerned that the incremental effort and related cost of the review will not be commensurate with any added audit quality. We agree that the concurring

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partner's attention should center on higher-risk areas and believe the existing concurring partner review requirements already address this objective.

- We are concerned about the impact the additional reviews required by the auditing firm may have on the timing of the Company's earnings releases and regulatory filings. The Company adheres to tight deadlines in order to complete the internal controls over financial reporting and provide sufficient time for management, the independent auditors and the Audit Committee to fulfill their responsibilities of a large accelerated filer.
- Finally, should this added regulation indeed move forward, we believe that a proposed implementation date for engagement reports issued on or after December 15, 2008 is too aggressive. We request providing a delay in the required effective date of the Release. We believe that the delay in the effective date will allow time for the public firms to address both implementation matters with their clients and resolve potential resource issues.

We appreciate this opportunity to comment. If you have any questions regarding this comment letter, please contact T. Mark Buford, Vice President, Corporate Controller and Chief Accounting Officer of Community Health Systems at (615) 465-7070.

Sincerely,



T. Mark Buford
Community Health Systems
Vice President, Corporate Controller and Chief Accounting Officer

cc: Larry Cash, Executive Vice President, Chief Financial Officer and Director

TMB/sct

Donald G. DeBuck
Vice President and Chief Financial Officer

May 12, 2008

Office of the Secretary
Public Company Accounting Oversight Board
1666 K Street, N.W., 9TH Floor
Washington, DC 20006-2803

Re: PCAOB Rulemaking Docket Matter No. 25, “Proposed Auditing Standard – Engagement Quality Review and Conforming Amendment to the Board’s Interim Quality Control Standards”



FILED ELECTRONICALLY (comments@pcaobus.org)

Dear Board Members and Staff,

Thank you for the opportunity to comment on the Public Company Accounting Oversight Board’s (the “Board”) proposed rule, “Proposed Auditing Standard – Engagement Quality and Conforming Amendment to the Board’s Interim Quality Control Standards” Release No. 2008-002 (the “Proposed Standard”), which was issued February 26, 2008. We commend the Board on its comprehensive efforts to involve all relevant constituencies in formulating this auditing standard.

We have supported the efforts of the President, Congress and the Securities and Exchange Commission to enhance investor confidence in the integrity of our financial reporting system. Accurate and reliable financial information is fundamental to investor confidence, and quality audits are an essential component of the US financial reporting system. As a result, auditing standards which address audit quality are critical to high standards for audits of public companies and sustaining the improvements to the financial reporting system in the United States realized through the regulatory refinements enacted under Sarbanes-Oxley.

While the Proposed Standard may help improve audit quality, it is only one of several ways through which audit quality is achieved and it is important to maintain the proper balance between the cost of these measures and resulting benefits. We are gravely concerned the Proposed Standard, in fact, will result in unintended consequences and significant costs, wholly disproportionate to the resulting benefits. Accordingly, we think the Board should use every possible means to mitigate the cost of these measures to registrants and, ultimately, investors.

- We are greatly troubled by what appears to be a fundamental change in the level of assurance expected to be achieved from the engagement quality

review, one which we believe is inherently inconsistent with the essential nature of the concurring review process.

- We have significant concerns regarding the exhaustive scope of required procedures which must be performed by the engagement quality reviewer and the prohibitively high cost of these audit procedures without commensurate benefits.
- We also believe the desired level of assurance, scope of procedures and documentation required under the Proposed Standard could significantly impact the timing of the final stages of an audit which could adversely impact the timeliness of issuer filings.
- Finally, we think the issues requiring reconsideration are so significant and pervasive that we suggest the Board reissue the Proposed Standard upon revision for further public comment to give adequate consideration to the viewpoints of all affected constituencies.

We have provided further information regarding these concerns, as well as other significant comments, concerns and suggestions, in the following paragraphs. We also have included detailed responses in Exhibit I to the specific questions for which the Board is seeking comment.

Engagement Quality Review: Level of Assurance

We are greatly troubled by what appears to be a fundamental change in the level of assurance expected to be achieved from the engagement quality review, one which we believe is inherently inconsistent with the essential nature of the concurring review process. Under the PCAOB Interim Standards, concurring review procedures are designed to enable the reviewing partner to express negative assurance. This requires the reviewing partner to deny his concurrence if, in the course of his procedures, he concludes that any matters have come to his attention which would cause him to believe the audit had not been performed in accordance with the audit standards of the PCAOB or the financial statements had not been prepared in conformity with generally accepted accounting principles.

The Proposed Standard attempts to increase the level of assurance by applying what is more nearly a legal standard but one which is not practicable. The Proposed Standard would require the reviewer to deny his concurring approval of issuance of the report if he knows or should have known “(1) the engagement team failed to obtain sufficient competent evidence in accordance with the standards of the PCAOB, (2) the engagement team reached an overall inappropriate conclusion on the subject matter of the engagement, the firm’s report, if a report is to be issued, is not appropriate in the circumstances, or the firm is not independent of its client.” We do not believe this level of assurance is consistent with the overall objective of a concurring review process.

Scope of Required Procedures

Procedures required under the Proposed Standard are far more exhaustive than practicable or necessary to achieve the necessary assurance. Review of all high risk areas of the engagement for a global client would not only be duplicative but would likely not be feasible. A scope this exhaustive could potentially require a parallel global engagement team working directly under the supervision of the quality reviewer. This would not only result in substantial additional cost without commensurate benefit but could also significantly and adversely impact audit timing and the timeliness of issuer filings with the SEC.

Review of Engagement Documentation

The review of engagement documentation would be substantially more expansive than currently required and could, in addition to the scope of procedures, present formidable challenges in practice. We believe the resulting delays and costs would greatly exceed the resulting benefit. We suggest the documentation subject to review include memoranda which summarize the relevant engagement matters, such as engagement planning; materiality and risks; significant accounting, auditing and financial reporting matters; high-risk transactions and balances; summary of unadjusted audit differences; management's report on internal control over financial reporting; and audit independence.

Qualifications of the Engagement Quality Reviewer

It is not entirely clear whether the Board intended to raise the level of competency required to perform the role of engagement quality reviewer. The Proposed Standard could be interpreted to require that the engagement quality reviewer possess the same level of knowledge as the engagement partner. This would unquestionably result in resource constraints, particularly in view of the concurring reviewer rotation requirements. We recommend the Proposed Standard incorporate less prescriptive guidance and allow greater professional judgment in determining the necessary qualifications for the role.

Independence, Integrity and Objectivity

Strict interpretation of the proposed requirements relating to objectivity could be interpreted to imply that:

- The engagement quality reviewer may not consult with specialists used by the engagement team as they may not be considered objective.
- These requirements may discourage timely consultation with the engagement quality reviewer.
- Existing audit practice management responsibilities, such as the roles of professional practice director, partner-in charge of the audit practice within an office, or global engagement partner, may be construed as supervising the

engagement team and therefore ineligible to function as the engagement quality reviewer despite the fact that these practice roles would not appear to interfere with their objectivity.

As a consequence we believe further clarification is necessary to avoid the foregoing unintended consequences.

Cost Benefit Considerations

We think the costs under the Proposed Standard do not appear to be reasonable in relation to the benefits to be achieved. Based on discussions with representatives of national public accounting firms, we believe the full cost of these requirements has been greatly underestimated. In addition to the cost implications, we believe there could be fairly serious resource constraints and timing issues.

Applicability

The applicability of the Proposed Standard to the auditor's review of interim financial information is not entirely clear since the standard is more narrowly framed in the context of an audit. Further clarification of the application of these requirements to audit procedures of interim financial information may be beneficial.

In addition, the Board has indicated it intends the Proposed Standard to apply to attestation engagements, in addition to audits. Since attestation engagements are governed by the attestation standards, we suggest the Proposed Standard be incorporated directly into, and as a part of, the PCAOB attestation standards, in addition to inclusion in PCAOB audit standards.

Transition

The Proposed Standard would be effective for reports issued after December 15, 2008. We do not believe the proposed transition would afford auditors sufficient time to address the process and resource challenges which the Proposed Standard would entail, particularly in view of the timing surrounding the public exposure process of the PCAOB and SEC. We recommend these requirements under the Proposed Standard be effective for engagements beginning one year after issuance of the Proposed Standard.

We thank you for the opportunity to express our views in this letter. If you have any questions or would like to further discuss our comments, please feel free to contact me at (310) 615-1686.

Sincerely,

Donald G. DeBuck

Chief Financial Officer

cc:

Mr. Mark W. Olson, Chairman
Mr. Daniel L. Goelzer, Board Member of the PCAOB
Mr. Bill Gradison, Board Member of the PCAOB
Mr. Charles D. Niemeier, Board Member of the PCAOB
Mr. Thomas Ray, Chief Auditor

Exhibit 1

Response to the Questions Set Forth in PCAOB Release No. 2008-002, “Proposed Auditing Standard – Engagement Quality Review” (the “Proposed Standard”)

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?

We believe it would be helpful to include an objective. In our view, the objective should be to provide a reasonable level of assurance the engagement team has performed their examination in accordance with PCAOB auditing standards, the financial statements have been prepared in accordance with generally accepted accounting standards and the audit report is appropriate in the circumstances.

We are greatly troubled by what appears to be a fundamental change in the level of assurance expected to be achieved from the engagement quality review, one which we believe is inherently inconsistent with the essential nature of the concurring review process. Under the PCAOB Interim Standards, concurring review procedures are designed to enable the reviewing partner to express negative assurance. This requires the reviewing partner to deny his concurrence if, in the course of his procedures, he concludes that any matters have come to his attention which would cause him to believe the audit had not been performed in accordance with the audit standards of the PCAOB or the financial statements had not been prepared in conformity with generally accepted accounting principles.

The Proposed Standard attempts to increase the level of assurance by applying what is more nearly a legal standard but one which is not practicable. The Proposed Standard would require the reviewer to deny his concurring approval of issuance of the report if he knows or should have known “(1) the engagement team failed to obtain sufficient competent evidence in accordance with the standards of the PCAOB, (2) the engagement team reached an overall inappropriate conclusion on the subject matter of the engagement, the firm’s report, if a report is to be issued, is not appropriate in the circumstances, or the firm is not independent of its client.” We do not believe this level of assurance is consistent with the overall objective of a concurring review process.

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

We think the engagement quality review should be required for all engagements subject to PCAOB auditing or attestation standards.

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

It is not entirely clear whether the Board intended to raise the level of competency required to perform the role of engagement quality reviewer. The Proposed Standard could be interpreted to require that the engagement quality reviewer possess the same level of knowledge as the engagement partner. This would unquestionably result in resource constraints, particularly in view of the concurring reviewer rotation requirements. We recommend the Proposed Standard incorporate less prescriptive guidance and allow greater professional judgment in determining the necessary qualifications for the role.

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?

We feel it is critical for the engagement team to confer timely with the engagement quality reviewer as matters arise throughout the course of the audit to facilitate expeditious conclusion of the audit, as well as timely issuer filings with the SEC. We believe such consultation contributes to the quality of the audit and does not in any way compromise their objectivity.

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

Procedures required under the Proposed Standard are far more exhaustive than practicable or necessary to achieve the necessary assurance. Review of all high risk areas of the engagement for a global client would not only be duplicative but would likely not be feasible. A scope this exhaustive could potentially require a parallel global engagement team working directly under the supervision of the quality reviewer. This would not only result in substantial additional cost without commensurate benefit but could also significantly and adversely impact audit timing and the timeliness of issuer filings with the SEC.

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 a risk-based approach but feel the scope of procedures under the Proposed Standard is overly broad, burdensome and unnecessary to achieve the objective of the engagement quality review.

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

The review of engagement documentation would be substantially more expansive than currently required and could, in addition to the scope of procedures, present formidable challenges in practice. We believe the resulting delays and costs would greatly exceed the resulting benefit. We suggest the documentation subject to review include memoranda which summarize the relevant engagement matters, such as engagement planning; materiality and risks; significant accounting, auditing and financial reporting matters; high-risk transactions and balances; summary of unadjusted audit differences; management's report on internal control over financial reporting; and audit independence.

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

We concur with the proposed timing of the engagement quality review.

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

As mentioned in our response to Question 1 above, we strongly feel a negative assurance standard would be more appropriate to the objectives of the engagement quality review process.

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

We think the guidance regarding documentation of the engagement quality review is not sufficiently clear and could potentially result in significant duplication of documentation prepared by the engagement team. This could further exacerbate potential issues surrounding audit timing and timeliness of issuer filings with the SEC mentioned in our response to Question 5 regarding the overly broad scope and extent of engagement quality review procedures.

11. 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 would be appropriate?

We think documentation of the engagement quality review should generally be subject to the same documentation principles generally applicable to the balance of the audit. However, we feel clarification may be necessary to avoid duplication.



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May 12, 2008

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RE: PCAOB Rulemaking Docket Matter No. 025, *Engagement Quality Review and Conforming Amendment to the Board's Interim Quality Control Standards*, PCAOB Release No. 2008-02

Office of the Secretary:

Crowe Chizek and Company LLC appreciates the opportunity to comment on the Public Company Accounting Oversight Board's ("PCAOB" or "Board") Proposed Auditing Standard, *Engagement Quality Review and Conforming Amendment to the Board's Interim Quality Control Standards* (the "Proposed Standard"). This letter contains our general comments on the Proposed Standard; responses to specific questions included in the Proposed Standard are in an Appendix to this letter.

The concurring reviewer responsibility included in the PCAOB's interim standards provides a meaningful periodic objective review of audit process performance and client financial reporting. The concurring review process adds some assurance to audit quality control. We applaud the Board's objective of providing greater clarity to the requirement for such engagement reviews, and believe that one result of clarity will be greater consistency in application both within firms and throughout the profession. The proposed requirement that all registered firms that perform audits of issuers conduct engagement quality reviews is a needed enhancement to the interim standards.

Expansion of Scope of Reviews

The Proposed Standard would greatly increase the scope, level of responsibility, and cost of performing the engagement quality review process. Specifically, the requirements for reviews at interim periods regardless of risk assessment, the new and expanded procedures required throughout the Proposed Standard, and the significant increase in level of responsibility to a "should have known" standard of care all result in large increases in the scope of engagement quality reviews. Any expansion of auditing procedures may provide improvement in quality. However, we believe the significant increased level of effort to perform the engagement quality review required by the Proposed Standard does not provide benefit to investors or preparers commensurate with the increased costs inherent in the Proposed Standard.

Omission of Stated Objective

The Proposed Standard does not contain a clear objective that articulates the purposes of the engagement quality review. An objective is essential, and consistent with principles based standard setting. Without a clearly stated objective of the purpose of the review, the consistency of review which is desirable may not be obtained. A stated objective will give reviewers guidance to assist in understanding and accomplishing the requirements. We believe that any final standard should include an objective which acts as a framework to conduct the review required by the standard. The framework for the objective should include the importance of using professional judgment in deciding what to review and the extent of review.

Standard of Performance – “know or should have known”

The Proposed Standard establishes a new standard of performance for an engagement quality reviewer, know or should have known, which is a significant increase in the level of responsibility for a reviewer. To perform at this level the reviewer will need to develop knowledge and judgment comparable to a second engagement partner. Also, the Proposed Standard requires independent evaluations instead of reviews of decisions made by the engagement team, even though the reviewer normally does not have comparable information and knowledge as the engagement team has. The focus of an engagement quality review standard should be on reviewing the significant judgments made and conclusions reached by the engagement team, not on developing a second set of independent conclusions. The expansion to a “should have known” level of performance changes the nature of the review from negative assurance to positive assurance by the reviewer. The focus on independent evaluations and positive assurance turns the focus of the audit to the engagement quality review rather than on the conclusions and judgments of the engagement team.

The engagement partner must have the ultimate responsibility for the audit. The engagement quality reviewer should not become an integral part of the engagement team, and should not have a level of responsibility comparable to the engagement partner, including overall responsibility for the audit. Unlike the engagement team members, the engagement quality reviewer's access to client records is limited, and they likely do not have routine interaction with the client. The need for independence and objectivity in this function, as well as the practical limitations on the scope of the engagement quality review, prevent the reviewer from forming the necessary judgments and conclusions to re-perform many of the evaluations and decisions made during the audit.

Documentation

The Proposed Standard contains new requirements relative to documentation. We believe that any documentation requirement should be limited to assessing the adequacy of documentation which was reviewed in connection with the limited procedures performed in accordance with the Proposed Standard. A final standard should not include a requirement that the engagement quality reviewer evaluate whether audit documentation is consistent with AS 3, as that is not consistent with the overall objective of an engagement quality review. Appropriate documentation is a result of systems design, audit strategy, training, supervision and significant

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 Page 3

teamwork throughout the audit, and is not the result of effort by one or a few personnel. This provision of the Proposed Standard would essentially create a pre-issuance compliance review of AS 3 requirements, a duty that should rest with the engagement team and reliance on overall firm processes.

International Standards Convergence

The review process included in the Proposed Standard is more extensive than that required by international auditing standards promulgated by the International Auditing and Assurance Standards Board. Divergence from international auditing standards may not serve to enhance audit quality, and may impede convergence of standards which is viewed as important for users to gain the benefit of a globally accepted set of standards.

Effective Date

We believe the effective date provided in the Proposed Standard should be changed. The effective date proposed is for engagement reports issued on or after December 15, 2008. A final standard would likely not be effective until some time in the second half of 2008. Most issuer audit engagements will have substantial services performed prior to a final standard becoming effective. The changed responsibilities of the engagement quality reviewer would be in effect for services already rendered, and the review timing desirable under the Proposed Standard would not be operable. Firms will also need time to implement the new requirements, including training, review of and potentially changing assignment of engagement quality reviewers to be compliant with new requirements. We suggest that the effective date be for periods beginning on or after six months after a final standard is approved by the SEC, and in no event sooner than for fiscal years beginning on or after January 1, 2009.

* * * * *

Crowe Chizek and Company LLC supports the Board's efforts to improve its auditing standards with the objective of furthering the public interest. We hope that our comments and observations will assist the Board in its consideration of the Proposed Standard. We would be pleased to discuss our comments with members of the Public Company Accounting Oversight Board or its staff. If you have any questions on our comments, please contact Wes Williams.

Cordially,



Crowe Chizek and Company LLC

Appendix

This Appendix provides responses to specific questions included in the Proposed Standard.

A. Engagements for Which an Engagement Quality Review Is Required

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?*

Yes. The Proposed Standard does not contain a clear objective that articulates the purposes of the engagement quality review. An objective is essential, and consistent with principles based standard setting. Without a clearly stated objective of the purpose of the review, the consistency of review which is desirable may not be obtained. A stated objective will give reviewers guidance to assist in understanding and accomplishing the requirements. We believe that any final standard should include an objective which acts as a framework to conduct the review required by the standard. The framework for the objective should include the importance of using professional judgment in deciding what to review and the extent of review.

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 required?*

No. Engagement quality reviews should be required for annual audits of financial statements and internal control over financial reporting. We do not believe that engagement quality review of reviews of interim information is warranted, given the cost of that review compared to the likely benefit. The availability of consultation between the engagement team and the engagement quality reviewer on significant matters or matters identified that raise the risk of material misstatement is sufficient for reviews of interim information.

Firm policy can require or suggest engagement quality review for any engagement where the judgment of the firm and/or engagement team deems that a review would add quality and value to the engagement. This is consistent with the risk associated with engagements and the needs of users. Our letter also addresses this matter.

B. Qualifications of the Engagement Quality Reviewer

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

The qualifications are appropriately described. We agree with the Board that engagement quality reviews do not always require a partner or equity owner, and that others may be well qualified to perform the reviews. However, we recommend that the reference in paragraph 2 to "another individual in the firm" be amplified to make clear that engagement quality reviews can be performed by non-partner level personnel that meet the qualifications provided in the Proposed Standard.

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?*

Yes. Consultation between the engagement team and the engagement quality reviewer should not only be allowed but should be encouraged. This can only lead to improvement in the

quality of the audit. Typical consultations would not impair the reviewer's objectivity. Consultations could be informal dialogue as well as formally documented matters.

C. The Engagement Quality Review Process

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?

No. Many of the requirements specified require the reviewer to "evaluate" judgments and decisions made by the engagement team, and to make "determinations". The requirements are so expansive that reviewers may conclude that they need to re-perform judgments that the engagement team and/or the engagement partner have made. Further, some of the required procedures are essentially a compliance check on parts of the audit, such as being sure that required communications were performed. Our letter also addresses this matter.

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?

The risk-based approach is an appropriate method to conduct an engagement quality review. The difficulty in the requirement of the Proposed Standard is that the approach prescribed requires all the procedures required by paragraphs 7 and 8, which procedures require the reviewer to re-perform judgments already made by the engagement team as described in the response to Question #5.

2. Review of Engagement Documentation

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

No. The engagement quality reviewer should not be responsible for determining if the engagement team has complied with AS 3.

The requirement in paragraph 10.c. that the engagement documentation "Supports the conclusions reached by the engagement team" may drive reviewers to review all audit documentation for significant risk areas, so they can provide the required positive assurance on that reviewed area. This level of review and assurance is greater than an engagement quality review should encompass.

3. Timing of the Review

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

Yes

D. Concurring Approval of Issuance

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

No. The standard of “know, or should know” is not appropriate. “Should know” relates to matters unknown to the reviewer. This is the most problematic provision in the Proposed Standard. The final standard should provide that the reviewer’s conclusion to approve issuance of a report be based on negative assurance after completing the procedures and scope of review required by the standard. Our letter also addresses this matter, and we do not repeat those comments here.

The Proposed Standard uses a concept of “concurring approval of issuance” in paragraphs 12 and 13, which is derived from The Sarbanes-Oxley Act provision that the reviewer express “concurring approval of its [the report] issuance.” We agree that audit reports subject to engagement quality review should not be issued until the engagement quality review is completed and documented, and that the reviewer should have the authority to perform the extent of procedures deemed necessary and not provide concurrence until they are satisfied that the report should be issued. However, we do not believe this should result in the engagement quality reviewer having a position equivalent to the engagement partner in approving the issuance of a report. Any final standard should be clear that the responsibility for determining whether the engagement is complete, which would include documentation of the engagement quality reviewer’s concurring approval for issuance, and that a report may be issued, should be the engagement partner’s alone.

E. Documentation of an Engagement Quality Review

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

The documentation requirements in paragraph 14 appear appropriate. The requirement for contemporaneous documentation of “When the review procedures were performed” will present challenges in application as the review requirements of the Proposed Standard will need to be performed multiple times, and perhaps continuously, throughout the period.

Paragraph 15 is not needed as it is a reminder that the audit documentation required by this standard would need to be retained like any other audit documentation. We do not believe repeating requirements of existing standards in new standards is helpful or adds clarity.

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?*

No.



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May 12, 2008

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**Re: PCAOB Rulemaking Docket Matter No. 025
Proposed Auditing Standard—Engagement Quality Review**

Deloitte & Touche LLP (“D&T”) is pleased to respond to the request for comments from the Public Company Accounting Oversight Board (the “PCAOB”) on its *Proposed Auditing Standard on Engagement Quality Review*, PCAOB Rulemaking Docket Matter No. 025 (Feb. 26, 2008).

If you have any questions or would like to discuss these issues further, please do not hesitate to contact Robert Kueppers at (212) 492-4241, James Schnurr at (203) 761-3539, or John Fogarty at (203) 761-3227. We thank you for your consideration of this matter.

Very truly yours,

/s/ Deloitte & Touche LLP

cc: PCAOB
Mark W. Olson, Chairman
Daniel L. Goelzer, Member
Bill Gradison, Member
Charles D. Niemeier, Member
Thomas Ray, Chief Auditor and Director of Professional Standards

SEC
Christopher Cox, Chairman
Paul S. Atkins, Commissioner
Kathleen L. Casey, Commissioner
Conrad Hewitt, Chief Accountant
Dr. Zoe-Vonna Palmrose, Deputy Chief Accountant for Professional Practice

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I. INTRODUCTION

D&T strongly supports the function of engagement quality review (“EQR”) and is committed to an effective EQR that promotes audit quality, focuses on significant judgments made and conclusions reached by the engagement team, and preserves the benefits that EQR provides as an objective review of the financial statements and the audit reports thereon. D&T recognizes that, with the adoption of a new standard, the responsibilities of audit firms with respect to EQR will change to some degree and that an increase in procedures performed and level of resources may be appropriate and necessary based on a new standard. As explained below, however, we have significant reservations about several aspects of the PCAOB’s proposed standard on EQR (*Proposed Auditing Standard on Engagement Quality Review*, PCAOB Rulemaking Docket Matter No. 025 (Feb. 26, 2008) (the “Proposal”). The Proposal would depart from current and international standards and practices, and impose obligations that would not bring corresponding improvements in audit quality and, in several respects, would be unworkable.

First, the Proposal would dramatically recast the standard for concurring approval, imposing a “knows, or should know” standard. Second, the extent of procedures contained in Paragraphs 8, 9, and 10 of the Proposal could result in a significant expansion in the scope of EQR and fundamentally change the manner in which EQR is conducted, without a commensurate benefit to audit quality. Taken together, these proposed requirements would likely impose unduly harsh consequences, including: (1) increasing the level of responsibility and of associated risk for EQR reviewers; (2) increasing the amount of time, effort, and resources needed to conduct an EQR; (3) unnecessarily increasing audit costs; and (4) making it difficult to issue reports in a timely manner. The Proposal would have EQR reviewers conduct procedures that duplicate in many respects those performed by the engagement team, and that far

exceed the procedures that are required by existing professional auditing standards and the proposed international standards for a concurring review. As a result, the Proposal dramatically alters the nature and function of EQRs.

In these respects, the Proposal also is at odds not only with the interim standard, but with the proposed international standards for EQR and the efforts toward and recognized advantages of a convergence of global standards and development of a single set of standards.¹ *See, e.g.,* Bill Gradison, PCAOB Member, Remarks at Conference of the American Accounting Association Public Interest Section and the Academy of Accounting Historians (Apr. 11, 2008) (suggesting “that we move towards ‘convergence’ (or, if you prefer, ‘harmonization’) with International Standards of Auditing”). The final EQR standard should avoid creating unwarranted, substantive differences in standards that govern the profession.

D&T’s comments on the Proposal, as set forth below, reflect the judgment and experience of numerous partners within D&T, including a significant number of partners who currently perform EQRs. We first provide our general comments on the Proposal, and then provide responses to the specific questions contained in the Release. In so doing, we suggest alternatives that we believe should be effective in promoting audit quality through EQR, while avoiding costly and unwieldy implementation problems.

¹ The proposed international standards are intended to “facilitat[e] the convergence of international and national standards, thereby enhancing the quality and uniformity of practice throughout the world and strengthening public confidence in the global auditing and assurance profession.” *See* Int’l Auditing & Assurance Standards Bd., *Terms of Reference ¶¶* 1.0-3.0 (Mar. 2006).

II. GENERAL COMMENTS

A. The PCAOB Should Adopt An EQR Standard That Is Based On Current Practices And The Proposed International Standards.

Concurring review, or EQR, has long been recognized as an integral part of the audit process, and standard setters and audit firms have expended considerable efforts through the years to establish high-quality EQR processes. The PCAOB's efforts to develop a new EQR standard therefore do not take place in a vacuum, but in the context of existing domestic and international standards and practices. *See* PCAOB Release No. 2008-002, at 5 (Feb. 26, 2008) ("Release"). The PCAOB's existing interim standard on concurring review was adopted from the American Institute of Certified Public Accountants ("AICPA") SEC Practice Section requirements, which embody professional standards that have long served public companies and investors. *See* SEC Practice Section §§ 1000.08(f), 1000.39 (Appendix E) ("Interim Standard"). Concurrent with the PCAOB Proposal, international authorities are advancing proposed changes to auditing standards and quality control standards encompassing EQR that also reflect longstanding practices. *See* Proposed Redrafted Int'l Standard on Auditing (ISA) 220, *Quality Control for an Audit of Financial Statements* (Int'l Auditing & Assurance Standards Bd. 2007) ("Proposed ISA"); Proposed Redrafted Int'l 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* (Int'l Auditing & Assurance Standards Bd. 2007) ("Proposed ISQC").²

² *See also* Int'l Standard on Auditing (ISA) 220, *Quality Control for Audits of Historical Financial Information* (Int'l Auditing & Assurance Standards Bd. 2006); Int'l Standard on Quality Control (ISQC) 1, *Quality Control for Firms that Perform Audits and Reviews of*

[Footnote continued on next page]

These proposed international standards have garnered widespread support in the European Union, Asia, and the United States (e.g., by the AICPA’s Auditing Standards Board). *See, e.g., Kelly Ånerud, Harmonization of Financial Auditing Standards in the Public and Private Sectors—What Are the Differences?*, *Int’l Journal of Gov’t Auditing* (Oct. 2007). Indeed, the PCAOB consulted the proposed international standards in developing its Proposal, and has noted various similarities. *See* Release at 5, 9 n.17, 13; *see also* Thomas Ray, PCAOB Chief Auditor and Director of Professional Standards, Remarks at PCAOB Board Meeting (Feb. 26, 2008) (in developing the Proposal, “the staff evaluated the Board’s interim requirement and the similar requirements of the International Auditing and Assurance Standards Board, the IAASB, of the International Federation of Accountants, and the AICPA auditing standards board”).

Collectively, these standards, the professional experience upon which they draw, and the guidance that has developed around them reflect several interrelated principles that should guide the formulation of the PCAOB’s final EQR standard. First, concurring review serves an important, yet limited purpose: to provide an “objective ‘second look’ at the engagement.” Release at 2; *see also* Robert D. Potts, Exchange Act Release No. 39,126, 1997 WL 690519, at *1 (Sept. 24, 1997) (opinion of the Commission) (concurring review provides a “second level of review”). Second, consistent with this limited purpose, a concurring reviewer’s responsibility should not be the same as the audit engagement partner’s responsibility. This is because, in part, “[i]n most cases, the concurring reviewer lacks an opportunity to review all of the client’s records, engage in discussions with the client’s management, or observe the client’s actions and

[Footnote continued from previous page]

Historical Financial Information, and Other Assurance and Related Services Engagements (Int’l Auditing & Assurance Standards Bd. 2006).

attitudes.” *See, e.g., Barry C. Scuttilo*, 74 S.E.C. Docket 1944, 2001 WL 461287, at *2 n.3, *48 (May 3, 2001) (stating also that there is “no accounting literature to suggest that . . . a concurring reviewer’s responsibility is the equivalent of the audit engagement partner’s responsibility”).

Third, and also consistent with this limited function, as the PCAOB has recognized, “the engagement quality reviewer’s role is not to perform procedures amounting to a re-audit.”

Release at 16; *see also Scuttilo*, 2001 WL 461287, at *48 (the concurring reviewer “is not expected to do the audit all over again”); *Potts v. SEC*, 151 F.3d 810, 813 (8th Cir. 1998) (“[A] concurring reviewer is not expected to do the audit all over again”), *cert. denied*, 526 U.S. 1097 (1999). Accordingly, in this “second-level review,” the concurring reviewer is not responsible “for searching out additional matters to be considered by the engagement team” that the engagement team did not itself identify in the course of the audit. *Scuttilo*, 2001 WL 461287, at *2 n.3, *48.

B. The Proposal Would Depart From Existing Standards And Could Fundamentally Change The Nature And Function Of EQR.

An EQR is and ought to be an objective, second-level review. The Proposal, however, departs from this precept in several important ways. First, the Proposal includes a “new standard” for concurring approval that is different from the interim standard and the proposed international standards. Release at 16 (“The proposal would establish a new standard that the engagement quality reviewer must meet in order to provide a concurring approval of issuance.”). Among other things, the new standard would require EQR reviewers to arrive at a conclusion based not only on what they know, but also on what they “should know.” In our view, this is unworkable.

Second, additional procedures mandated by the Proposal would dramatically expand the scope of an EQR, increasing audit costs and presenting challenges for completing audits in a

timely manner. The costs associated with the expanded scope of EQR are compounded when considered in light of the manner in which reviews would necessarily be conducted if a “should know” standard is imposed. EQR reviewers will feel compelled to move beyond the “second look” role they now perform, and move instead to performing many of the same procedures performed by the engagement team. This would seemingly be inconsistent with the PCAOB’s stated view—which we share, and which is consistent with current practices and the proposed international standards—that “the engagement quality reviewer’s role is not to perform procedures amounting to a re-audit.” *Id.*³

1. The Proposed “Knows, Or Should Know” Standard Represents An Unprecedented Departure From Current Practices.

Under the proposed international standards, as well as current practices, the EQR reviewer’s conclusion is based on what has come to the reviewer’s attention during the course of the review—that is, what the reviewer *actually knows* based on the procedures performed. Based on this knowledge, the EQR reviewer provides assurance that the reviewer is not aware of any audit or other relevant deficiencies. Proposed ISA 220, ¶ 27; Proposed ISQC 1, ¶ 49; Interim Standard at section (b). This level of assurance is appropriate given the objective of an EQR and the extent of the procedures that an EQR reviewer should be expected to perform. Under the Proposal, however, the EQR reviewer would be required to provide assurance based not only on

³ If the PCAOB ultimately decides to adopt the Proposal, the PCAOB should state more clearly why it has elected to chart a different course. We recognize that, in formulating its standard, “the Board considered information on this topic from PCAOB inspections” and “findings from recent PCAOB enforcement cases,” Release at 4; however, the PCAOB has not described findings that would justify imposing such a dramatically different approach to EQR. Nor has the PCAOB presented findings on why the deficiencies it says it has identified are best addressed by a new EQR standard rather than recommending other quality-control measures.

what the reviewer knows, but also on what the reviewer *should know*. Proposal ¶ 12. This represents a significant recasting of the EQR reviewer’s role, which heightens the level of responsibility for EQR reviewers and would have profound implications for the conduct of EQR.⁴ The significance of the shift to the “knows, or should know” standard is illustrated by the fact that this standard is not currently used in PCAOB auditing and professional standards—even for the engagement partner—including in those standards developed in the first instance by the PCAOB (e.g., PCAOB Auditing Standard (AS) No. 5).

The “should know” standard is illogical—and thus unworkable—because a reviewer cannot reasonably be asked to make a representation (e.g., provide a concurring approval) based on what he or she “should know,” as opposed to what the reviewer actually knows. This is not to suggest that what an EQR reviewer actually knew may not later be reviewed by a third party, who may assert, in retrospect, that the reviewer could have done more work and should have known more on which to have based the earlier concurring approval.⁵

Also disconcerting is the inexorable link between a level of assurance premised on what the reviewer “should know” and the expanded scope of the EQR reviewer’s responsibilities

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- ⁴ This increased responsibility would be accompanied by an increased level of exposure. Although it may be argued that this risk could be mitigated by reliance on more procedures—a position that is itself in tension with the concept of EQR—in a highly litigious environment, the “should know” standard will inevitably distort the conduct of EQRs.
- ⁵ While the SEC applies a form of a “knows, or should know” standard in evaluating cases of alleged professional misconduct under SEC Rule 102(e), the Rule 102(e) analysis is meant to discern the degree of departure from the underlying professional standard; it does not itself purport to describe the conduct prescribed and proscribed by the standard. Consequently, by way of example, the Staff of the SEC may inquire on a retrospective basis whether, in making a judgment with respect to an issuer’s receivables, the auditor should have known—and was reckless in not knowing—more about the aging of the receivables. But generally accepted auditing standards do not require an auditor to base conclusions on what he or she “should know.”

under the Proposal. As discussed in the next section of this letter, the scope of procedures to be performed by the EQR reviewer is greatly expanded. At the same time, there are various ambiguities as to just what is required, and the EQR reviewer will exercise significant judgment in determining what work to do. Specifically, the Proposal’s “should know” language captures information that would be obtained as a result of performing the extensive procedures described in Paragraphs 7 through 10 of the Proposal,⁶ procedures that suggest that the EQR reviewer should acquire the same, or a substantially similar, depth of knowledge about the audit as the engagement partner. Consequently, the scope of what a reviewer “should know” when providing concurring approval may appear to some EQR reviewers to be virtually without bounds, and they will feel compelled to perform a broad array of additional procedures in order to obtain more and more information and to discourage second-guessing about whether the EQR reviewer knew enough.

This incentive to conduct such protective procedures raises several concerns. Performing additional procedures would be more time consuming and would impose additional costs. The time required to perform these procedures, combined with the expanded scope of review as described in the Proposal, will impose a heavy additional burden on EQR reviewers. This additional work will fall squarely on the shoulders of the EQR reviewer, who retains overall responsibility for the EQR. Release at 10. The significant increase in the amount of work to be performed, and the responsibility of providing concurring approval under the “should know”

⁶ While Paragraph 7 appropriately reflects EQR as it is now conducted—and as it is contemplated by the proposed international standards—Paragraph 9, Paragraph 10, and parts of Paragraph 8 add significantly to the task as discussed in Section II.B.

standard, may cause reluctance on the part of those who will be called upon to conduct EQR reviews to participate in the EQR process.

Finally, these protective procedures would be inconsistent with the current understanding of the EQR as a “second look.” They also would run counter to the PCAOB’s expressed goal that an EQR reviewer is not to “perform procedures amounting to a re-audit.” *Id.* at 16. Indeed, the degree of involvement that would be necessary to meet the “knows, or should know” threshold would affect the ability of the EQR reviewer to take that necessary “step back” and conduct the review from the perspective of an outsider “looking in.” *Id.* at 10.

We agree with the PCAOB that an EQR reviewer should conduct a more limited second-level review that is conducted by taking a “step back,” rather than a review that, in effect, duplicates much of the work of the engagement partner. But that is not how the Proposal has been drafted. To address this disconnect, the PCAOB should adopt the following language in lieu of Paragraph 12; this language retains the Proposal’s structure while narrowing the scope of the EQR reviewer’s determination to the significant facts that have come to the reviewer’s attention during the EQR:

The engagement quality reviewer must not concur with the issuance of an engagement report if, based on information that comes to his or her attention in his or her review in accordance with this standard, the reviewer believes that (1) the engagement team failed in any material respect to obtain sufficient competent evidence in accordance with the standards of the PCAOB, (2) the engagement team reached an inappropriate overall conclusion on the subject matter of the engagement, (3) the firm’s report, if a report is to be issued, is not appropriate in the circumstances, or (4) the firm is not independent of its client.

In the alternative, the PCAOB should adopt the IAASB’s standard, under which EQR reviewers must state that they are “not aware of any unresolved matters that would cause [them] to believe that the significant judgments the engagement team made and the conclusions they reached were not appropriate.” Proposed ISA 220, ¶ 27; Proposed ISQC 1, ¶ 49.

If the PCAOB declines to adopt either of the above approaches, the Proposal—at a minimum—should be modified to omit the “should know” language to reflect that the EQR reviewer’s knowledge of the audit is necessarily limited to what the reviewer has learned based on the procedures required to be performed and that the reviewer cannot reasonably be asked to make a representation based on what he or she “should know.” In short, the EQR reviewer’s responsibility should not extend beyond the scope of the reviewer’s actual knowledge.

2. The Proposal Could Significantly Increase The Scope Of EQR Without A Commensurate Benefit To Audit Quality.

The scope and extent of the procedures contained in Paragraphs 8, 9, and 10 of the Proposal would likely result in substantial changes to the existing scope of EQR and the manner in which it is conducted. Specifically, Paragraph 8 contains a long list of “procedures” that the EQR reviewer should conduct during the course of a review, some of which extend beyond current practice. Moreover—and separate from the additional procedures provided for in the paragraph—because many of the proposed “procedures” are vaguely worded, the resulting uncertainty as to what work must be done would add significantly to the work performed under current practices and the proposed international standards. Paragraph 9 requires EQR reviewers to supplement their EQR procedures with an additional “risk-based” analysis, but its scope is also unclear, and it would lead to the performance of unintended, unnecessary or redundant procedures. Finally, Paragraph 10 requires an extensive review of engagement team working papers that is not consistent with the limited role of an EQR. Each of these issues is discussed in more detail below.

Also, contrary to the PCAOB’s expectation that the Proposal would avoid unnecessary costs, *cf.* Release at 6 (“[T]he Board . . . endeavored to draft a standard that would avoid imposing any unnecessary costs.”), the scope of the Proposal as described above would require

significantly more time, effort, and resources to complete a qualifying EQR, and would lead to significant increases in audit costs.⁷ The additional time would have to be expended largely by the EQR reviewers themselves, many of whom are among our most experienced partners. They constitute a resource whose availability is limited and which would be extremely difficult to augment in the short term.⁸ The PCAOB's expectation that the Proposal would impose only minimal incremental costs is without foundation.

a. Paragraph 8 Appears To Expand Areas Subject To Review.

Paragraph 8 of the Proposal sets forth ten broad “procedures” that EQR reviewers are expected to complete as part of conducting the EQR. Many of them are vaguely described; there is little guidance as to how they are supposed to be conducted; and collectively, they would significantly expand the scope of the review. Both subparagraphs 8(a) and 8(b), for example, require the EQR reviewer to “[o]btain an understanding” of various audit-related matters, including the audit firm’s relationship with the client and the client’s significant financial reporting issues and risks. Each of these represents a significant undertaking, and is more an objective than a procedure. In any event, the Proposal does not explain how the EQR reviewer is to obtain such understandings. “Obtain an understanding” is a broad concept that could be viewed to require the EQR reviewer to undertake—at a minimum—an exhaustive review of the

⁷ Based on our experience, we estimate that the Proposal, as written, would require the EQR reviewer to spend significantly more time on EQR—likely a multiple of the number of hours that are spent under current practices. Additionally, other members of the engagement team are likely to spend additional time as a result of the increased scope of the EQR and increased responsibilities of the EQR reviewer.

⁸ Based on data from our internal time reporting system, audit partners (which includes individuals serving as engagement partners and/or EQR reviewers) worked on average approximately sixty hours per week from the middle of January through the first week of March 2008. Significantly increasing the workload for these same individuals during this time frame would detract from audit quality rather than improve it.

working papers and other materials not in the working papers, and to conduct extensive interviews with a broad array of engagement team members and possibly client personnel. Absent guidance, it will be difficult for the EQR reviewer to determine what steps are sufficient to meet the requirements.

In the face of this uncertainty, the EQR reviewer may feel compelled to perform all procedures that the standard could be interpreted to require, and thereby unnecessarily expend time, effort, and resources on an EQR that goes well beyond what the PCAOB may have intended. These expanded efforts would be at odds with the proposed international standards, current practices, and the PCAOB's Release, which provide that EQR is, and should remain, a limited second-level review. *See, e.g., Scutillo*, 2001 WL 461287, at *2 n.3, *48; Proposed ISA 220, ¶¶ 20-23; Proposed ISQC 1, ¶¶ 42-44; Interim Standard at section (b); Release at 2.

The PCAOB should revise the requirements of Paragraph 8, and provide guidance as to the scope of its various subparts, so that it is consistent with the established tenets of concurring review. A more extensive discussion of the specific provisions of Paragraph 8 and the clarifications we recommend are set forth in Section III.D.

b. Paragraph 9 Requires Additional And Unnecessary Analysis.

Paragraph 9 of the Proposal states that the EQR reviewer “should assess whether there are areas within the engagement that pose a higher risk that the engagement team has failed to obtain sufficient competent evidence or reached an inappropriate conclusion.” As drafted, Paragraph 9 is subject to different interpretations and could be read to impose requirements that are largely duplicative of other provisions of the Proposal and thus unnecessary.

First, Paragraph 9 could be read to focus the EQR inappropriately on an assessment of, and the risks associated with, the engagement team's performance as opposed to the areas of risk that exist in the client's financial statements. Focusing on possible shortcomings of the

engagement team would detract from consideration of the areas of the financial statements that present the greatest risk of material misstatement, and would not be an effective means of improving audit quality. Such a focus also could unnecessarily generate a tension between the engagement team and the EQR reviewer that would be counterproductive to the EQR and the audit. The EQR reviewer should be perceived as a resource for enhancing audit quality, not as an intrusive factor interfering with the audit in real time.

Second, current practice requires the EQR reviewer to “review . . . matters that were considered significant by the engagement team in conducting the audit” and provides that “the concurring partner reviewer is not responsible for searching for additional matters to be considered by the engagement team.” Interim Standard at section (b). By contrast, this interpretation of Paragraph 9 would effectively require that the reviewer undertake to identify audit risks that were not identified by the engagement team. A requirement to look for unidentified risks would place the EQR reviewer in the shoes of the engagement partner and have him or her re-perform the risk identification and assessment process on the engagement. Such a process would further increase the level of effort required to perform an appropriate EQR, is inconsistent with the concept of concurring review, and is unnecessary to achieve the objectives of EQR.

Third, Paragraph 7, with its focus on evaluating the engagement team’s “significant judgments” and pertinent conclusions, already focuses the EQR reviewer’s attention on the most important aspects of the audit, and in so doing embodies an adequate risk-based approach. Paragraph 8, as discussed above, already contains an extensive catalog of procedures to be followed and objectives to be achieved. To the extent Paragraph 9 adds another layer to the EQR process, it would be redundant and costly. Indeed, in light of the extensive procedures separately

required by other aspects of the Proposal, Paragraph 9 is inconsistent with a true risk-based approach that aims to “center the engagement quality reviewer’s attention on higher-risk areas” because it would have the EQR reviewer focus on so many areas, regardless of the perceived risk. *See* Release at 6.

For these reasons, Paragraph 9 does not appear to advance a true risk-based approach. To the contrary, it could seriously detract from an efficient and effective risk-based approach focused on the areas of higher-risk. We therefore recommend omitting Paragraph 9 from the final standard and including language specifying that the EQR reviewer should discuss with the person having overall responsibility for the engagement, any previously unidentified risks that have come to the attention of the EQR reviewer as a result of performing the procedures in Paragraphs 7 and 8. (This language could be incorporated into Paragraph 7.) This would result in a standard that is more consistent with the proposed international standards. *See, e.g.,* Proposed ISA 220, ¶ 20; Release at 13 (noting that Paragraph 7’s “requirement to evaluate significant judgments is similar to the requirements of the related standards of the IAASB”).

c. Paragraph 10 Adds Extensive Documentation Review Requirements.

The Proposal would increase the obligations of EQR reviewers even further by requiring an extensive review of audit documentation, an undertaking that also is contrary to basic precepts of concurring review. Paragraph 10 of the Proposal requires the EQR reviewer to evaluate the audit documentation relating to all “matters that were subject to” the EQR procedures, which is a substantially different and broader set of materials than the documentation the EQR reviewer currently reviews in connection with the EQR procedures. Such matters would include all of the areas encompassed by Paragraphs 7, 8, and 9, which, as described above, together would significantly expand the EQR reviewer’s obligations independent of the documentation review

requirement. Consequently, Paragraph 10's documentation evaluation requirement could be interpreted broadly to require the EQR reviewer to review *virtually all of an audit's underlying working papers*. That simply would be impractical. An EQR reviewer would typically need a team of reviewers to gain comfort that the Proposal's requirements have been satisfied. This level of proposed document review would present significant challenges for timely completing EQRs, and, as a result of the resources needed to accomplish the document review, the Proposal would increase audit costs.

The Paragraph 10 review also requires the EQR reviewer to determine whether the applicable engagement team's documentation "[i]s appropriate in the circumstances and consistent with the requirements of PCAOB Auditing Standard No. 3, *Audit Documentation* ('AS No. 3')." Such a documentation review by the EQR reviewer would be duplicative of the review performed by the engagement partner, who has primary responsibility for the performance of the audit and who must be satisfied that the audit documentation contains sufficient appropriate audit evidence. Further, although the auditor must have completed the EQR prior to the release of the auditor's report (Proposal ¶ 11), and "must have completed all necessary auditing procedures and obtained sufficient evidence to support the representations in the auditor's report," the final assembly of audit documentation is not required to be completed until forty-five days *after the report is issued*. AS No. 3, ¶ 15. This sequence will affect the EQR reviewer's ability to assess fully the sufficiency of what appears to be virtually all of the audit's underlying working papers—including those that may not yet have been finalized. We recommend that the PCAOB modify the final standard to make it clear that the EQR reviewer should exercise professional judgment in selecting for review the working papers that relate to the significant judgments the engagement team made and the conclusions it reached—which, as a practical matter, are

completed *before* the issuance of the audit report—and to recognize that certain working papers that are selected for review may not yet have been finalized. This approach would be consistent with AS No. 3 and the proposed IAASB standards. *See* Proposed ISA 220, ¶ 21; Proposed ISQC 1, ¶ 44.

In the alternative, the Proposal should identify specific documents to be reviewed during an EQR—for example, the financial statements, the engagement completion document, and other documents provided to the EQR reviewer by the engagement team that, in the EQR reviewer’s judgment, relate to significant judgments made and the conclusions reached.

3. The Proposed Effective Date Is Unworkable And Should Be Modified.

The PCAOB has proposed that the standard be effective “for engagement reports issued . . . on or after December 15, 2008.” Release at 18. This effective date is unworkable for several reasons. First, because the PCAOB contemplates that EQR be “conducted contemporaneously with the engagement,” *id.* at 2, a fully compliant EQR simply cannot be conducted for an engagement that is underway before the final standard is issued. Consistent with the PCAOB’s expressed preference for contemporaneous EQR, concurring review procedures are conducted throughout the course of the engagement. Therefore, for fiscal years that have begun prior to issuance of the final standard, it is not reasonable to expect that EQRs will have been conducted pursuant to an unreleased final standard. In addition, even engagements that are currently being planned cannot be expected to anticipate the requirements of the final standard. The PCAOB should adopt an effective date that is tied to the beginning of an engagement period, which will allow audit firms to plan and implement an EQR that complies with the final standard from the start of an engagement to its conclusion.

The effective date also could cause other transition issues. If the proposed effective date (i.e., for reports issued on or after December 15, 2008) is adopted in the final standard, it appears that, if a report is re-issued after the effective date, and the EQR of the audit was performed under the prior standard, then the report would not be in compliance with the requirements of the standard. The PCAOB should clarify that this is not its intent.

Furthermore, the Proposal's new and extensive requirements make it very unlikely that firms could change their practices in time to meet the December 15, 2008 effective date. To allow compliance with the requirements of the standard, as proposed, D&T would have to train its partners and professional employees, re-deploy resources, and create the tools necessary to assist in the conduct of a compliant EQR. There would not be sufficient time to implement these steps.

For these reasons, the new EQR standard should apply to audit reports issued for fiscal years beginning twelve months after the date the SEC approves the final standard. This would allow sufficient lead time to take necessary measures to comply with the requirements of the standard, and would minimize the impact of the other transition issues addressed herein.

III. RESPONSES TO SPECIFIC QUESTIONS

The specific issues on which the PCAOB has sought comments are discussed below. In several of these areas, we suggest alternative approaches that we believe will serve the PCAOB's goals while avoiding costly or unwieldy implementation problems. Many of these suggestions are based on the proposed international standards that address EQR. While we generally support consistency between PCAOB standards and the proposed international standards, we also recognize that the United States regulatory environment makes additional guidance and specificity appropriate in particular circumstances identified below.

A. The Proposal Should State An Objective.

Question No. 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?

Stating an objective would provide a yardstick against which the final standard's effectiveness can be measured, and would facilitate an understanding of the standard's provisions. An objective therefore would be of assistance both to those implementing the standard and those enforcing it. We suggest that the PCAOB adopt the following:

The objective of the EQR is to provide for an independent, objective consideration of significant auditing, accounting, and financial reporting matters, including significant judgments made and conclusions reached by the engagement team, to determine whether the EQR reviewer concurs with the issuance of the engagement report.⁹

This recommendation is consistent with the prevailing understanding of concurring review as a "second look" and that "the engagement quality reviewer's role is not to perform procedures amounting to a re-audit." Release at 16. By focusing the EQR on "significant" matters, it makes clear that the EQR reviewer is not to perform substantive procedures or a complete inspection of the engagement team's work, and thus distinguishes between the roles of engagement partner and EQR reviewer. The language we propose contemplates that the EQR reviewer will question and challenge the engagement team's judgments where appropriate, and reach a conclusion whether to concur based on the relevant facts and circumstances of which the reviewer has knowledge.

⁹ "[S]ignificant auditing, accounting, and financial reporting matters" is defined in the interim standard as "matters involving a significant risk of material misstatement of financial statements, including a material disclosure deficiency in the footnotes to the financial statements." Interim Standard at introduction n.2.

Finally, the proposed objective is consistent with the concept of EQR as one integral part of a broader system of quality control, including engagement performance, firm-wide monitoring, and retrospective reviews. This proposed objective thus is also consistent with the proposed international standards. Proposed ISA 220, ¶¶ 20-23 (delineating a complementary but separate role for the concurring review partner vis-à-vis the engagement partner); Proposed ISQC 1, ¶¶ 42-44 (same).

B. The Application Of The Proposal To Interim Reviews And Attestation Engagements Should Be Modified.

Question No. 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 required?

We believe that EQR should be required on all engagements performed in accordance with the PCAOB's standards. As discussed below, however, the PCAOB should modify the intended application of the Proposal to interim reviews and attestation engagements. First, consistent with the more limited scope and objective of a review of interim financial information, the EQR procedures performed for such reviews should similarly be circumscribed. Second, an EQR requirement for attestation engagements should not be codified among the PCAOB's audit standards, but should be made part of the PCAOB's attestation standards.

1. Interim Reviews

We agree that EQR procedures should be performed in connection with reviews of interim financial information. The Proposal, however, does not differentiate between the EQR procedures to be performed for audits of annual financial statements and for reviews of interim financial information, even though the objective, scope, and degree of assurance provided by interim reviews are obviously different from those of audits. As the PCAOB is aware, interim

reviews are limited in scope and consist of procedures that are significantly narrower than those performed in an audit. As discussed in PCAOB Interim Standard AU 722.07, interim reviews consist principally of performing certain analytical procedures and making inquiries. Several of the procedures set forth in the Proposal cannot be reconciled with the work performed for a review of interim financial information. Engagement planning, for example, including the related identification of fraud risks and planned audit responses to them, often will not be completed at the time a review of a company's first quarter financial statements is performed and concurred upon. Nevertheless, the Proposal appears to require concurring review procedures related to such engagement planning. *See, e.g.*, Proposal ¶¶ 8-10. In some respects, the Proposal appears to require the EQR reviewer to obtain more evidence and to provide a higher level of assurance than the engagement team when performing a review of financial statements. This is not appropriate, and presumably unintended.

The PCAOB, therefore, should limit the breadth of EQR procedures required for interim reviews and should modify the conclusion to be reached by the EQR reviewer in connection with such interim reviews. Specifically, the PCAOB should include in the final standard an additional section, analogous to Paragraph 7, that states that the EQR reviewer, in a review of interim financial information, should “discuss significant matters identified and addressed in connection with the [interim] review.”

Similarly, the final standard should require that only certain procedures set forth in Paragraph 8 (specifically those set forth in subparagraphs 8(g), 8(h), and 8(i), as revised pursuant to the suggestions herein) be completed for interim reviews. Finally, the standard should clarify

that the EQR reviewer is required to provide only a level of assurance of concurring approval that is consistent with the overall conclusion of an interim review.¹⁰

2. Attestation Engagements

The Release states that the proposed audit standard would apply to *attestation* engagements, such as agreed-upon procedure engagements. *See* Release at 8. The PCAOB, however, has separate attestation standards. *See* Interim Attestation Standards § 101 *et seq.* (PCAOB 2003). Accordingly, any EQR standard that is intended to apply to attestation engagements should be proposed in connection with, and adopted separately and incorporated within, those separate attestation standards. It is counterintuitive to include requirements for attestation engagements within the auditing standards. We therefore recommend that any final EQR audit standard not apply to attestation engagements. This change to the PCAOB’s Proposal would ensure that the practitioners performing attestation engagements under PCAOB standards would be aware of the relevant requirements, avoiding confusion. It also would ensure that any standard that eventually may be adopted for attestation engagements is appropriately tailored to the unique aspects of those engagements.

C. The Proposed Qualifications Of The EQR Reviewer Require Clarification.

Question No. 3. Are the qualifications of an engagement quality reviewer appropriately described in the proposed standard? If not, how should they be revised?

We agree that EQR reviewers should exhibit “competence, independence, integrity, and objectivity.” Proposal ¶ 3. These attributes are cornerstones of the auditing profession. We are

¹⁰ This modification is more consistent with the Sarbanes-Oxley Act of 2002, which contemplates a concurring review only for audit reports, not interim reviews. *See* 15 U.S.C. § 7213(a)(2)(A)(ii) (“concurring or second partner review and approval of such *audit report*”) (emphasis added).

concerned, however, that the Proposal’s descriptions of the “competence” and “objectivity” requirements, in particular, could lead to confusion and difficulties in implementation, undermining the PCAOB’s goal to “establish more clearly the level of expertise and experience that is necessary to perform an objective engagement quality review.” Release at 9. First, we believe that the “competence” requirement may be interpreted to require that the EQR reviewer and the engagement partner have the identical knowledge and skills. Second, we believe that the “objectivity” requirement, as proposed, could be read to prohibit common—and important—EQR reviewer tasks, including consulting with members of the engagement team. Each of these concerns can be readily addressed.

1. Competence

The Proposal requires that the EQR reviewer “possess the level of knowledge and competence related to accounting, auditing, and financial or other reporting *required to serve* as the person who has overall responsibility for the same type of engagement.” Proposal ¶ 4 (emphasis added). The Release provides that “competence” would encompass not only technical accounting, auditing, and financial reporting expertise, but also specialized industry knowledge: “For example, a person assigned to perform the engagement quality review for an audit of a public company engaged in oil and gas exploration and development should have experience *sufficient to serve* as the engagement partner for the audit of a public company in this specialized industry.” Release at 9 (emphasis added). The phrases “required to serve” and “sufficient to serve” in the Proposal are likely to be interpreted to require the EQR reviewer to have the *same* level of competence—that is, technical expertise *and* specialized knowledge—as the engagement partner. This goes beyond the interim standard, which requires “sufficient technical expertise and experience to achieve the purposes” of the concurring review, and which “contemplates knowledge of relevant specialized industry practices.” Interim Standard at section (a).

The Proposal essentially requires that a “clone” of the engagement partner be selected to be the EQR reviewer; however, it will not always be possible for the EQR reviewer to have the same qualifications or same level of experience and expertise as the engagement partner. It is not realistic to expect an EQR reviewer, who may conduct a number of reviews each year for clients in different industries, to acquire the same degree of in-depth knowledge regarding the business of each client as the engagement partner, whose role requires more time focusing on the business of a particular audit client. As businesses become increasingly specialized, it will become even more difficult to identify EQR reviewers with sufficiently specialized knowledge to meet the Proposal’s test. Moreover, there may be times when an EQR reviewer without substantial knowledge of the relevant specialized industry may be better suited to conduct an EQR than someone with specialized knowledge, perhaps because he or she has particular expertise or experience dealing with the accounting principles that are implicated by issues likely to arise in the audit. Or, to take another example, a partner who has experience in serving a quality control function within the firm (and as a result is highly skilled at addressing the risks associated with a particular engagement) may be best suited in a particular case to be the EQR reviewer, even though this person may not have experience in the particular industry. An EQR reviewer’s years of experience and breadth of knowledge are valuable resources that should not be diminished by focusing solely on technical expertise and industry expertise. Audit firms should have sufficient discretion to match the skills of the EQR reviewer with appropriate audits.

The difficulty in identifying enough EQR reviewers to satisfy the Proposal’s definition of “competence” is compounded by existing auditor independence requirements relating to the rotation of audit partners. Both the engagement partner and the concurring review partner must rotate off an engagement after five years of service and may not act as an EQR reviewer on that

engagement in the following five years. *See* 17 C.F.R. § 210.2-01(c)(6)(i).¹¹ The rotation rules thus limit the pool of candidates who may serve as an EQR reviewer. In addition, the office that conducts the audit often also conducts the EQR until a rotation occurs. If there is not another partner in that office who can conduct the EQR, it must then be assigned to partners in other offices. This poses obstacles to communication and coordination that make EQR more difficult to perform effectively. Adding to these challenges by requiring that the EQR reviewer have the same degree of technical expertise *and* specialized knowledge as the engagement partner would further limit the pool of potential EQR reviewers.¹²

The final standard should dispel any notion that the engagement partner and the EQR reviewer must have the same degree of technical expertise and specialized knowledge, and make it clear that audit firms may exercise discretion in assigning EQR reviewers based on the facts and circumstances of the particular engagement. This can be accomplished most readily by stating in Paragraph 4 that “considerations in evaluating competence include, but are not limited to, technical expertise, experience, knowledge of SEC rules and regulations pertinent to the engagement, and industry knowledge,” and by incorporating into the final standard Footnote 18 of the Release, which states that competence should be assessed “based on the circumstances of

¹¹ Under this rule, an individual may serve as the engagement partner for three years, and then as EQR reviewer for two years, before rotating off the engagement for five years. The interim standard adds an additional rotation requirement that “a prior audit engagement partner should not serve as the concurring partner reviewer for at least two annual audits following his or her last year as the audit engagement partner.” Interim Standard at section (a).

¹² Indeed, the requirement that audit partners rotate off of an engagement makes it more difficult to acquire and maintain the degree of specialized knowledge that appears to be contemplated by the Proposal. The Proposal appears not to recognize the significance and effect of the rotation requirement.

the engagement, including the size or complexity of the business.” Consistent with these changes, the PCAOB also should omit the example on page 9 of the Release regarding EQR for an oil and gas exploration and development company. *See* Release at 9 n.18. This approach also would be consistent with the proposed IAASB standards. *See, e.g.*, Proposed ISQC 1, ¶ A42 (“What constitutes sufficient and appropriate technical expertise, experience and authority depends on the circumstances of the engagement.”).

2. Objectivity

The Proposal requires the EQR reviewer to perform the review with objectivity. *See* Proposal ¶¶ 3, 5, 6. In order to preserve objectivity, the EQR reviewer is not to “make decisions on behalf of the engagement team, assume any of the responsibilities of the engagement team, or supervise the engagement team.” *Id.* ¶ 6 (formatting omitted). Again, we agree that the reviewer must approach the prescribed tasks objectively. However, as discussed below in response to Question 4, the Proposal may discourage the EQR reviewer from obtaining information through consultations with members of the engagement team, potentially undermining the quality of the EQR. The Proposal also may discourage communications between a client’s management and/or audit committee and the EQR reviewer that can serve to enhance audit quality. Finally, the Proposal departs from the proposed international standards. We recommend revisions to address these issues below.

a. Consultations With The Engagement Team

Question No. 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?

We believe that the standard should not only allow but *encourage* consultations between the engagement team and the EQR reviewer. Such consultations are likely to foster more timely and effective auditing on the part of the engagement team members by bringing to bear the

experience and expertise of the EQR reviewer on matters under discussion. Frequent consultations increase the likelihood that issues that should be addressed in the audit will be identified more quickly. This is just one of many ways in which timely consultation between the engagement team and the EQR reviewer improves audit quality and allows for effective consideration of significant matters that arise during the course of an audit, and does so without adversely affecting the objectivity of the EQR reviewer.

For example, in situations involving complex accounting judgments, it is important for the engagement team to consult with the EQR reviewer throughout the audit process. Such consultations help the EQR reviewer to consider whether relevant issues and guidance have been considered, whether appropriate resources or specialists have been involved, and whether the engagement team has made appropriate judgments. They also help provide that the EQR reviewer's questions are properly addressed. Such consultations are particularly helpful when new accounting or auditing standards are being implemented—when the EQR reviewer may be able to provide unique insights based on knowledge of the firm's positions and on how those positions are applied in the firm's practice.

It may be particularly helpful for the EQR reviewer to discuss specific matters with specialists employed by the engagement team. When the EQR reviewer has questions regarding a complicated valuation issue, for example, the most knowledgeable person often is the valuation specialist who assisted the engagement team. Such consultations enable the EQR reviewer to understand the procedures performed, the judgments involved, and the conclusions drawn. The EQR reviewer's objectivity should not be questioned simply because of these consultations with the valuation specialist. Consultations between the engagement team and the EQR reviewer

ultimately contribute to audit quality, and should not be deemed to compromise the reviewer's objectivity with respect to the audit.

Although the Proposal does not prohibit consultations between the EQR reviewer and the engagement team, the standard contains language that could inappropriately discourage such communications. We recommend the revisions described below to clarify the acceptable bounds of reviewer-engagement team consultations.

i. Clarification Is Needed Regarding Consultations With The Engagement Team.

The note to Paragraph 6 provides, “[t]he engagement team may consult with the engagement quality reviewer on matters during the course of the engagement,” but goes on to warn that “[w]hen participating in such consultations, the engagement quality reviewer should not participate in a manner that would compromise his or her objectivity with regard to the engagement.” (Emphasis added). Neither the Proposal nor the Release specifies what it means to participate “in a manner that would compromise his or her objectivity” As a result, the emphasized provision may have the unintended consequence of discouraging beneficial communications between the engagement team and the EQR reviewer. We therefore recommend omitting the emphasized language in the note to Paragraph 6.

ii. The Proposal's Definition Of "Objectivity" Could Cause Confusion.

Paragraph 5 of the Proposal requires that the EQR reviewer “maintain objectivity with respect to the engagement *and the engagement team.*” (Emphasis added). Notwithstanding contrary text in the note to Paragraph 6, this language could be read to prohibit the EQR reviewer from consulting with members of the engagement team (or specialists employed by the engagement team) to supplement his or her knowledge regarding specialized issues in connection with an engagement. Footnote 19 of the Release reinforces this concern by warning that the

EQR reviewer may consult only with those who are “independent of the client, have integrity, and possess an appropriate level of competence and objectivity.” This language may discourage an EQR reviewer from speaking with a specialist who performed work for the engagement team because the specialist might not be considered to be “objective” with respect to that team. This could undermine the EQR and ultimately undermine audit quality. To avoid confusion, the final standard should omit Footnote 19 of the Release and clarify that the EQR reviewer is encouraged to consult with the members of the engagement team, including specialists, in order to gain an understanding about significant accounting and auditing matters relating to the engagement.

b. Communications With Management

The Proposal does not specifically contemplate communications between the EQR reviewer and management of the audit client. Without additional guidance, this omission could be interpreted as a change to current practices and discourage communications that can be beneficial to the client and the EQR reviewer. *See* Interim Standard at section (b) (providing for such communications under certain circumstances). The EQR reviewer can play an important role in facilitating candid and robust dialogue among the auditor, management, and the audit committee, allowing for a more effective audit. The Proposal should incorporate language to recognize that communications between the EQR reviewer and members of a client’s management and audit committee may take place.

c. Supervision Of Engagement Team

The Proposal would prohibit EQR reviewers from “[s]upervis[ing] the engagement team.” Proposal ¶ 6. This language departs from the proposed international standards. We suggest revising Paragraph 6 in accordance with the proposed IAASB standards, providing that objectivity may be maintained when the EQR reviewer “[d]oes not make decisions for the

engagement team” and “[d]oes not otherwise participate in the engagement during the period of review.” Proposed ISQC 1, ¶ A44.

D. The Proposal Could Be Read To Expand The Scope Of EQR Significantly.

Question No. 5. Are the descriptions of the scope and extent of the engagement quality review procedures contained in the proposed standard appropriate? If not, how should they be changed?

We addressed the substance of this question in Section II.B.2. above. There, we explained that the extent of the procedures contained in Paragraphs 8, 9, and 10 of the Proposal could result in substantial changes to the scope and manner of the conduct of an EQR, and we suggested alternative approaches better tailored to serve the goals of concurring review.

Below is a discussion of certain provisions of Paragraph 8, where we believe additional guidance is needed.

- Paragraph 8(a) requires the EQR reviewer to “[o]btain an understanding of the firm’s recent engagement experience with the company and risks identified in connection with the firm’s client acceptance and retention process.” However, the Proposal does not make clear how the EQR reviewer is to obtain that understanding, which makes it difficult for a reviewer to determine when he or she has completed steps sufficient to meet this requirement. Consistent with the existing standard and the proposed international standards, we therefore recommend that the PCAOB clarify this requirement by defining its parameters more precisely. Paragraph 8(a) should be revised to require the EQR reviewer to “obtain an understanding” of the risks identified as part of the firm’s client acceptance and retention process through “discussion with the engagement partner” and “review of selected working papers.” Proposed ISA 220, ¶ 21; Proposed ISQC 1, ¶ 44; Interim Standard at section (b).
- Paragraph 8(b) requires the EQR reviewer to “[o]btain an understanding of the company’s business, significant activities during the current year, and

significant financial reporting issues and risks.” As with Paragraph 8(a), it is not clear how the EQR reviewer is expected to achieve this objective. It could be difficult for the EQR reviewer to determine when he or she has acquired sufficient knowledge to fulfill the requirement. The final standard should make clear that the EQR reviewer can sufficiently obtain an understanding of the company’s business through “discussions with the engagement partner,” “review of certain working papers,” and performance of the other procedures enumerated in Paragraph 8.¹³

- Paragraph 8(c) requires the EQR reviewer to “[r]eview the engagement team’s evaluation of the firm’s independence in relation to the engagement.” Rather than setting forth steps to be performed, Paragraph 8(c) sets forth an objective to be achieved without explaining how to achieve it. We recognize that the proposed international standards include a similar requirement, *see* Proposed ISA 220, ¶ 22; Proposed ISQC 1, ¶ 45, but further clarification is needed in the context of the U.S. regulatory environment. The final standard should specify the independence issues that the EQR reviewer should evaluate. We believe the EQR should be limited to those issues that have been identified in the Independence Standards Board (ISB) Standard No. 1 letter, ISB Standard No. 1, *Independence Discussions with Audit Committees* (AICPA 1999), and such other matters deemed appropriate in the judgment of the EQR

¹³ Without clarification, this language may be interpreted similarly to the requirements under PCAOB Interim Standard AU 311.06: “The auditor should obtain a level of knowledge of the entity’s business that will enable him to plan and perform his audit in accordance with generally accepted auditing standards.” As a result, the EQR reviewer may interpret the Proposal as requiring extensive procedures similar to those performed by the engagement team in order to “obtain an understanding.” The Proposal’s “obtain an understanding” language should contain moderating language as proposed herein.

reviewer.¹⁴ The EQR reviewer should not be required to re-evaluate issues that are monitored through the firm's centralized independence compliance processes.

- Paragraph 8(f) requires the EQR reviewer to “[d]etermine if appropriate consultations have taken place on difficult or contentious matters” and to “[r]eview the documentation, including conclusions, of such consultations.” Again, the Proposal does not specify how the EQR reviewer is to achieve this objective. We recognize that there is a similar requirement in the proposed international standards; however, here again, in the context of the U.S. regulatory environment, we believe further clarification is needed. Otherwise, as written, the Proposal could be interpreted to require that the EQR reviewer undertake extensive review of the working papers in order to identify the “difficult or contentious matters.” The PCAOB should clarify this requirement by explaining that, *based on the EQR reviewer's understanding of the significant judgments made*, the EQR reviewer should consider whether appropriate consultations have taken place and review the related documentation of such consultations, including the conclusions.
- Paragraph 8(i) requires the EQR reviewer to “[d]etermine if appropriate matters have been communicated, or identified for communication to the audit committee, management, and other parties, such as regulatory bodies.” It is not clear how the EQR reviewer is supposed to determine whether all such appropriate matters have been communicated. Among other things, this requirement could be viewed to require the EQR reviewer to review a large volume of working papers. The PCAOB

¹⁴ The PCAOB recently adopted a new rule to replace ISB Standard No. 1. This new rule is substantially similar to ISB Standard No. 1 in many respects. *See* PCAOB Release No. 2008-003, at 1 (Apr. 22, 2008) (SEC approval pending).

should clarify that the EQR reviewer should consider, based on the procedures performed, whether appropriate matters have been communicated to management and the audit committee.

E. The Proposal Does Not Successfully Advance A “Risk-Based” Approach.

Question No. 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 addressed the substance of this question in Section II.B.2.b. As discussed, it is not clear what the PCAOB intended to accomplish through the “risk-based” assessment proposed in Paragraph 9. We expressed concern that Paragraph 9 focuses the EQR inappropriately on the *engagement team* performance, rather than on risk of material misstatement in the client’s financial statements. We also noted that a Paragraph 9 assessment would achieve the same objective as the Paragraph 7 evaluation of significant judgments, and constitute a redundancy without an incremental value to the audit. We therefore recommend omitting Paragraph 9 from the final standard and specifying, perhaps in Paragraph 7, that the EQR reviewer should discuss with the person with overall responsibility for the audit any previously unidentified risks that come to the attention of the EQR reviewer as a result of performing the procedures in Paragraphs 7 and 8.

F. The Requirement For The Review Of Engagement Documentation Is A Significant Change In Practice And Will Be A Time Consuming And Costly Process.

Question No. 7. Are the proposed requirements for the review of the engagement team’s documentation appropriate? If not, how should they be changed?

We addressed the substance of this question in Section II.B.2.c. While we recognize the need to provide that audits are appropriately documented, we noted that the Proposal would significantly increase the obligations of EQR reviewers by requiring an extensive review of audit

documentation that is contrary to the basic precepts of concurring review and would be duplicative of the engagement partner's responsibility.

We therefore recommend that the final standard make clear that the EQR reviewer should exercise professional judgment in selecting for review the working papers that relate to the significant judgments the engagement team made and the conclusions it reached. In the alternative, the Proposal should identify specific documents to be reviewed during an EQR—for example, the financial statements, the engagement completion document, and other documents provided to the EQR reviewer by the engagement team that, in the EQR reviewer's professional judgment, relate to significant judgments made and the conclusions reached.

G. Additional Work Required By The Proposal Will Make It Difficult To Meet Accelerated Filing Deadlines.

Question No. 8. Is the description of the timing of the engagement quality review, as proposed, appropriate? If not, how should it be changed?

Under the Proposal, an EQR reviewer must “complete his or her review prior to providing concurring approval of issuance.” Proposal ¶ 11. While we agree that the concurring approval should be completed prior to the issuance of the related report, as discussed in Section II.B.1.-2., the additional work required by the Proposal, including extensive review of audit documentation, together with the implications of the proposed “knows, or should know” standard—which collectively could require that the EQR reviewer conduct a review too closely resembling the audit procedures of the engagement team—would make it difficult for issuers and auditors to meet the accelerated filing deadlines. Accordingly, absent applicable changes to the standard, we recommend that the PCAOB confer with the SEC regarding issuers' ability to meet SEC filing deadlines and whether the deadlines, particularly for Form 10-K for large accelerated and accelerated filers, should be modified.

In addition, we have identified concerns with the proposed effective date, which are described above in Section II.B.3.

H. The Final Standard Should Not Adopt A “Should Know” Standard For Concurring Approval.

Question No. 9. Is the standard for the engagement quality reviewer’s concurring approval of issuance appropriate? If not, how should it be changed?

We addressed the substance of this question in Section II.B.1. There, we explained that the proposed “knows, or should know” standard goes well beyond traditional concepts of concurring review embodied in both the interim standard and the proposed international standards, and is unworkable in the context of an EQR reviewer reaching a conclusion. For the reasons discussed, a reviewer cannot be expected to provide concurring approval based on what he or she “should know.” We further explained that the Proposal would create an incentive to perform additional procedures in order to obtain information to blunt second-guessing about information that the EQR reviewer “should have known.” Such protective procedures would add disproportionately to the time and effort involved with the EQR and ultimately to audit costs. To address these concerns, the PCAOB should adopt the language proposed in Section II.B.1. In the alternative, the PCAOB should adopt the IAASB’s standard or, at a minimum, modify the standard to omit the “should know” language to reflect that the EQR reviewer’s knowledge of the audit is necessarily limited and that responsibility should not extend beyond the scope of the reviewer’s actual knowledge.

I. The EQR Documentation Requirements Are Unclear And Should Be Clarified.

Question No. 10. Are the documentation requirements for an engagement quality review appropriate? If not, how should they be changed?

Question No. 12.¹⁵ Should the proposed standard require documentation of the engagement quality review to comply with other provisions in AS No. 3? If so, which provisions should apply?

We appreciate the PCAOB's efforts at detailing EQR documentation requirements in Paragraphs 14 and 15. However, certain aspects of the Proposal, described below, should be clarified or modified to ensure that an EQR proceeds efficiently.

The PCAOB should clarify how detailed the required documentation is expected to be. For example, as currently drafted, subparagraphs (c) and (e) of Paragraph 14 require that EQR documentation include information regarding the procedures performed by the EQR reviewer and the "results of the review procedures." These subparagraphs could be interpreted to require the EQR reviewer to draft what is, in effect, a second audit summary memorandum. Such a requirement would be redundant and, by creating additional work, would delay the completion of the EQR and the issuance of the audit report, making it more difficult to meet filing deadlines. Moreover, we do not believe that increasing the documentation requirements for the EQR—in and of itself—is likely to improve audit quality. To the contrary, increased documentation requirements would distract the reviewer from important EQR procedures. The final standard should ensure that the reviewer's focus remains on the EQR rather than the documentation, and should clarify that the EQR reviewer is not expected to duplicate the work of the engagement team related to documentation. We believe that it is sufficient for the EQR reviewer to document that a review was done in compliance with the standard, and by whom, without the need for detailed listings of procedures performed and documentation reviewed.

¹⁵ The Release does not include a Question No. 11.

To this end, we recommend that the PCAOB adopt the IAASB's approach, which would require documentation that: (1) the procedures have been performed; and (2) the EQR has been completed before the [issuance] of the report. *See* Proposed ISA 220, ¶ 27; Proposed ISQC 1, ¶ 49.

If the PCAOB chooses not to adopt the IAASB's approach, it should make the following refinements to Paragraph 14 of the Proposal. Paragraph 14 requires that documentation of an EQR include information concerning, among other things, "[w]hen the review procedures were performed" and "[t]he results of the review procedures." First, regarding subparagraph (d), the PCAOB should clarify that the EQR documentation should provide: (1) the date the EQR was completed; and (2) the date on which concurring approval was provided. This recommendation reflects the fact that review procedures may be performed over a period of time, and the date on which the review was completed and the date on which approval was provided may be different. Second, we suggest that the phrase "results of the review procedure" in subparagraph (e) be replaced with the more specific phrase "conclusion reached as a result of the review procedures." The degree of detail with which one should specify "[t]he results of the review procedures" is difficult to discern. Without clarification, the term "results" could be interpreted broadly to require specific findings for each aspect of an audit (no matter how perfunctory or mundane), the totality of which composes the "conclusion." To achieve this level of reporting, the EQR reviewer likely would have to perform procedures similar to those that have been performed by the engagement team.

Finally, any final standard should make clear that the *only* provisions of AS No. 3 that apply to EQR documentation are those "related to retention of and subsequent changes to audit documentation." Proposal ¶ 15.

IV. CONCLUSION

While D&T supports efforts to strengthen EQR, we believe that the Proposal, in many respects, goes well beyond the established purpose of a concurring review; and together, these proposed requirements could have unnecessarily adverse consequences, including: (1) increasing the level of responsibility and associated risk imposed on EQR reviewers; (2) increasing the amount of time, effort, and resources required to conduct an EQR; (3) increasing audit costs; and (4) making it difficult to issue timely reports, all without providing a commensurate and corresponding improvement in audit quality. Nevertheless, we believe that the Proposal, if revised as we have suggested above and in light of the proposed international standards, could provide a substantial benefit to audit quality.



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12 May 2008

Proposed Auditing Standard–Engagement Quality Review and Conforming Amendment to the Board’s Interim Quality Control Standards; PCAOB Rulemaking Docket Matter No. 025

Dear Mr. Seymour:

We are pleased to comment on the Public Company Accounting Oversight Board’s (“PCAOB” or the “Board”) Proposed Auditing Standard–Engagement Quality Review (“the Proposed Standard”) and Conforming Amendment to the Board’s Interim Quality Control Standards (“the Proposed Amendment”), collectively referred to as “the Proposal.”

As a preliminary matter, we support the Board’s efforts to adopt a comprehensive standard consistent with Section 103 (a) (2) (A) (ii) of the Sarbanes-Oxley Act, which requires that the Board adopt a standard that registered public accounting firms “provide a concurring or second partner review and approval of [each] audit report (and other related information), and concurring approval in its issuance, by a qualified person (as prescribed by the Board) associated with the public accounting firm, other than the person in charge of the audit, or by an independent reviewer (as prescribed by the Board).” We also are of the view that engagement quality reviews are but one element of an overall system of quality control. Therefore, proposed changes to the Board’s interim standards should be considered in the context of a firm’s system of quality control taken as a whole.

An engagement quality review that focuses on significant judgments made and conclusions reached by the engagement team is effective in promoting audit quality. Because of the importance of this role, we also believe an engagement quality review should be required for every audit conducted pursuant to the standards of the PCAOB. We also believe ongoing consultations between the engagement team and the engagement quality reviewer are critical to the audit process. Therefore, we also agree that the engagement team should be permitted to consult with the engagement quality reviewer during the engagement, providing the engagement team and the reviewer do so in a manner that does not impair the reviewer’s objectivity.

We believe the final standard should state the purposes and objectives of the engagement quality review. It is critically important that regulators, investors, audit committees, and company management have a consistent understanding of the intent of the engagement quality review. Further, a clear articulation of the overall purpose and objective of the review will help auditors in applying professional judgment in determining the nature and extent of the review procedures to be

applied. A clearly stated objective also will aid in differentiating the role and function of the engagement quality reviewer from that of the engagement partner and other members of the engagement team.

We agree with the Board's view that "well-performed engagement quality reviews are an important element in establishing a basis for investor reliance on audits." However, despite our support for a comprehensive standard, we are concerned with the following aspects of the Proposed Standard that we believe will significantly change the nature and scope of the engagement quality review and will result in additional costs associated with such reviews without a corresponding benefit to audit quality.

Summary Views on the Proposed Standard

The Proposed Standard would significantly change the nature and scope of the engagement quality review. Since its inception as a membership requirement of the SEC Practice Section of the AICPA Division for CPA Firms, the engagement quality review has been a "fatal flaw" review with the stated objective of identifying potential matters that, if not addressed prior to issuance of the audit report, potentially would require recalling and reissuing the audit report when subsequently discovered. Under current PCAOB interim standards, the engagement quality reviewer can provide concurring approval so long as "no matters had come to his or her attention that would cause the [reviewer] to believe" that the financial statements did not conform to generally accepted accounting principles in all material respects or that the audit was not performed in accordance with generally accepted auditing standards. We believe that PCAOB inspection reports of both larger and smaller audit firms, for the most part, corroborate that engagement quality reviews performed under existing standards have accomplished this objective.

Furthermore and as more fully described in later sections of this comment letter, the Proposed Standard differs substantially from the requirements of international auditing standards promulgated by the International Auditing and Assurance Standards Board. We believe the final standard should more closely align with international standards, which would result in a more appropriate focus for the engagement quality review. Moreover, doing so would be consistent with the growing demand for convergence of world wide accounting and auditing standards and the broad-based recognition of the benefits of developing a single set of standards for worldwide use. We believe that further consideration should be given to the benefits of convergence and to avoiding the creation of unnecessary substantive differences in standards.

The Proposed Standard, when considered in its entirety, would require the engagement quality reviewer to determine that he or she has sufficient grounds to positively concur with the issuance of the audit report. In our view, this requirement would significantly expand the scope, effort, and related cost involved with performing the engagement quality review as it would require the reviewer to duplicate many aspects of the role and function of the engagement partner and other members of the engagement team and likely duplicate other firm-wide monitoring procedures. Under the Proposed Standard, the engagement quality reviewer would be compelled to develop separate determinations and judgments on significant matters rather than evaluate the significant judgments made and conclusions reached by the engagement team in the audit. This, in turn, would require that the reviewer acquire his or her own base of knowledge to make such determinations and judgments. Further, this requirement would shift the focus of the engagement quality review away from

identifying potential material misstatement(s) of the financial statements and determining whether the engagement team reached reasonable conclusions about significant matters and instead focus on the adequacy of the review itself and the basis for the reviewer's separate determinations. We do not believe this shift in focus would serve to enhance audit quality.

We also believe the Proposed Standard sets expectations, obligations, and performance standards for an engagement quality reviewer that practically would be very difficult to satisfy with a reasonable amount of effort. Because the engagement quality reviewer must maintain independence and objectivity and not assume responsibilities for the audit or supervise the engagement team, there is a difference in the nature of the information available to the engagement partner and the engagement quality reviewer. The engagement quality reviewer's conclusion will necessarily be based on a more limited amount of first hand knowledge. In our view, an engagement quality reviewer could interpret the Proposed Standard in such a way that results in the performance of significant additional work for the purpose of obtaining such first hand knowledge in order to establish grounds to positively concur with the issuance of the audit report. We believe the natural consequences of such interpretation would be the creation of an engagement quality review that, in many respects, duplicates the review procedures required of the engagement partner and results in measurable increases in costs associated with the independent review without corresponding enhancements to audit quality.

Views Relating to Paragraphs 9 and 10 of the Proposed Standard

Paragraphs 9 and 10 of the Proposed Standard require the engagement quality reviewer to (1) assess whether there are areas within the engagement that pose a higher risk that the engagement team has failed to obtain sufficient competent evidence or reached an inappropriate conclusion and (2) to evaluate, for those areas reviewed, the engagement team's documentation. These requirements would appear to conflict with paragraph 6, which prohibits the engagement quality reviewer from assuming responsibilities of the engagement team or supervising the engagement team. We believe the assessment of audit risk and preparation and review of audit documentation are core responsibilities of the engagement team under existing auditing standards.

Paragraph 3.c of PCAOB Auditing Standard No. 3, *Audit Documentation (AS3)*, states that an engagement quality reviewer reviews documentation to "understand how the engagement team reached significant conclusions." In our view, this reference in the PCAOB's existing guidance describes the engagement quality reviewer's appropriate role as an objective reviewer who does not assume responsibilities of the engagement team.

We note that the reference to "higher risk" in paragraph 9 is not directed to the potential for material misstatements or any other objective standard. Instead, the Proposed Standard instructs the engagement quality reviewer to "assess whether there are areas within the engagement that pose a higher risk that *the engagement team* has failed to obtain sufficient competent evidence or reached an inappropriate conclusion." We believe this incorrectly implies that the engagement quality reviewer should assess the ability of the engagement team to address the risks posed by the engagement rather than, or in addition to, reviewing the engagement team's assessment of the risks posed by the engagement. We believe this paragraph should be revised to focus the reviewer on determining whether certain "significant" matters, such as significant risks of material misstatement of the financial statements, might not have been previously identified by the engagement team.

We believe that preparation and review of audit documentation are core responsibilities of the engagement team under existing auditing standards. Paragraph 13 of AS3 requires that the engagement team “identify all significant findings or issues in an engagement completion document.” Paragraph 13 further states that “this document, along with any documents cross-referenced, should collectively be as specific as necessary in the circumstances for a reviewer to gain a thorough understanding of the significant findings or issues.” If the engagement team is required to prepare an engagement completion document and the primary purpose of that document is to facilitate an engagement quality review, then it would seem duplicative for the engagement quality reviewer, as proposed, to be required to evaluate the engagement team’s underlying documentation for matters that were subject to the engagement quality review procedures. In our view, a qualified engagement quality reviewer should be able to achieve the objectives for the engagement quality review by performing the procedures outlined in paragraphs 7 and 8 of the Proposed Standard, which reflect existing requirements and also would include reading the engagement completion document.

We also believe paragraph 10 of the Proposed Standard is impractical, particularly for multi-location engagements where engagement documentation is prepared by multiple global teams, many times in a variety of languages. Paragraph 19 of AS3 requires the office issuing the report to obtain, review and retain only certain items of the documentation related to the work performed by other auditors, including other offices of the firm or affiliated firms. Accordingly, it would not be possible for the engagement quality reviewer to evaluate whether documentation of the matters at all locations that were subject to the engagement quality review procedures is appropriate as indicated in paragraph 10. The engagement quality reviewer’s evaluation of engagement documentation would necessarily be limited to only those items of documentation forwarded to the office issuing the report.

In attempting to position the engagement quality review as the linchpin for a quality audit through the requirements of paragraphs 9 and 10, the Board has unnecessarily complicated the engagement quality review. In our view, these additional requirements would add time, effort and cost to the engagement quality review without a corresponding benefit in audit quality. In comparison to current practice, we do not believe that the requirements in paragraphs 9 and 10 of the Proposed Standard often would enhance the identification of significant matters previously unidentified by the engagement team, but rather might result in the identification of relatively insignificant or minor issues that do not justify attention beyond that given by the engagement team. We recommend that the Board modify the proposed requirements in paragraphs 9 and 10 to instead refocus on significant risks of material misstatement to the financial statements and significant difficult, judgmental, or contentious matters that either were identified and considered, or should have been identified and considered, by the engagement team. If such matters are found to exist that were not previously identified and considered by the engagement team, the engagement quality reviewer should be required to communicate these matters to the engagement team and assess whether the engagement team responds appropriately.

Views Relating to Paragraph 12 of the Proposed Standard

We are concerned that the “knows or should know based upon the requirements of this standard” language in paragraph 12 of the Proposed Standard will expose engagement quality reviewers to substantial risk of sanctions, either by the SEC or the PCAOB, in nearly every occasion where an audit is later found to be deficient. As discussed above, the engagement quality review process set forth in

paragraphs 7 through 11 of the Proposed Standard would impose significant new obligations on the reviewer, and given these obligations a reviewer may find it difficult to show that he could not have known about an audit deficiency. Thus, persons performing engagement quality reviews will interpret paragraph 12 to mean that they must be as informed, if not more informed, as the engagement partner before providing concurring approval of issuance. This acquisition of first hand knowledge would therefore entail significant additional involvement and effort by the engagement quality reviewer. He or she presumably would have to review the audit work and documentation for each high risk area in order to form his or her own conclusions on significant matters rather than rely on inquiries of engagement team members or review of summary documentation (e.g., the engagement completion document) prepared by the engagement team. When read in connection with paragraph 10, paragraph 12 could effectively require the engagement quality reviewer to review in considerable detail all key audit documentation for the areas selected for review as it would be presumed that the engagement quality reviewer “should know” whether there was a deficiency with the work that was performed, the documentation, or the conclusions.¹

This “should know” standard would doubtlessly result in increased time, effort, and cost for performing an engagement quality review. In this regard, the Release accompanying the Proposed Standard states that the Board has attempted to draft a standard that will avoid the imposition of “unnecessary costs,” but we do not believe that the obligation set on the engagement quality reviewer set forth in this paragraph of the Proposed Standard meets that objective.

Views Relating to Paragraph 4 of the Proposed Standard

We are concerned that the level of competence established in the Proposed Standard for the engagement quality reviewer is too precise and will unnecessarily limit the pool of individuals who could perform an engagement quality review. Paragraph 4 of the Proposed Standard states “the engagement quality reviewer must possess the level of knowledge and competence related to accounting, auditing, and financial or other reporting required to serve as the person who has overall responsibility for the same type of engagement (emphasis added).” In its Release accompanying the Proposed Standard at II.B.1. on page 9, the Board provides, as an example of the appropriate knowledge and competence of an engagement quality reviewer, a statement that a person assigned to perform the engagement quality review for an audit of a company involved in “oil and gas exploration” should have experience sufficient to serve as the engagement partner in this specialized industry. We are concerned that the requirements in the Proposed Standard and the example in the accompanying Release place too much focus on a specific type of engagement or specialized industry expertise. We recommend removing this example from the Release, and including a statement in paragraph 4 of the Proposed Standard that “considerations in evaluating competence include, but are not limited to, technical expertise, experience, knowledge of SEC rules and regulations pertinent to the engagement, and industry knowledge.”

¹ In this regard, the rulemaking record of Rule 3502, “Responsibility Not to Cause Violations,” is relevant. The Board originally proposed a rule that would have allowed the Board to impose discipline on a person associated with a registered accounting firm when that person “knew or should have known” that his or her actions would contribute to a violation by the registered firm. After reviewing comments on this proposal the Board determined to instead adopt a standard of “knowing, or recklessly not knowing” of the violation. We believe that here, with respect to engagement quality reviewers, the “should know” standard is similarly too low a threshold.

Also in the Release accompanying the Proposed Standard at II.B.1 on page 9, the Board indicates that “the proposed standard seeks to establish more clearly the level of expertise and experience that is necessary to perform an objective engagement quality review.” However, the Release does not provide the Board’s rationale for doing so, or indicate whether, in the Board’s view, the clearer delineation of the level of expertise and experience is intended to change current practice. We believe a clearer understanding of the degree to which the Board intends for the Proposed Standard to change current practice in the selection and assignment of engagement quality reviewers and the procedures to be performed when conducting an engagement quality review will aid auditors in developing or refining their policies and procedures.

Views Relating to Paragraph 14 of the Proposed Standard

We believe documentation of the engagement quality review should not be more extensive than documentation of other required reviews in the conduct of an audit. Engagement partners ordinarily sign and date those workpapers (e.g., analyses, memoranda, contracts and agreements, correspondence, audit programs) that were reviewed and additionally sign and date other checklists and practice aids to document other matters that were considered and other procedures that were performed. These sign-offs ordinarily provide relevant information about the matters listed in items a through f of paragraph 14 of the Proposed Standard. We further believe checklists and other standard practice aids are effective and efficient methods of determining that all required procedures have been performed and further believe such tools result in unequivocal approval (or non-approval) of issuance of the audit opinion.

Views Relating to Paragraph 8 of the Proposed Standard

Item i of paragraph 8 requires the engagement quality reviewer to “determine if appropriate matters have been communicated, or identified for communication to the audit committee, management, and other parties, such as regulatory bodies.” We believe the phrase “determine if appropriate matters have been communicated” could be interpreted by an engagement quality reviewer to mean he or she needs to be present when the communications are made. In our view, this expectation also conflicts with the prohibition in paragraph 6. We recommend that the final standard indicate that the reviewer should consider whether appropriate matters of which the engagement quality reviewer is aware have been communicated, or identified for communication to the audit committee, management, or other parties, such as regulatory bodies.

Views Relating to Applicability of the Proposed Standard

As currently drafted, the Proposed Standard would require an engagement quality review and concurring partner approval of issuance for each engagement performed and completed in accordance with the standards of the PCAOB. While we agree that it is appropriate for an engagement quality review standard to apply to all engagements performed in accordance with the auditing standards of the PCAOB, the requirements in the Proposed Standard are so specifically tailored to audits of financial statements or integrated audits of financial statements and internal control over financial reporting, that it would be difficult to apply the Proposed Standard to other types of engagements with any consistency. For example, the Proposed Standard does not specifically state what the responsibilities of the engagement quality reviewer would be in an interim review or how the

review procedures would differ. It might be appropriate to presume that certain requirements do not apply (for example, reading management's report on internal control would not apply in a review of interim financial information). However, in other situations, the Board's intent is less clear.

We recommend that the final standard address the Board's intent regarding the application of this standard to engagements other than financial statement audits and integrated audits. We believe the final standard initially should only apply to financial statement audits, to integrated audits, and—providing the final standard clarifies how the standard should be implemented—to reviews of interim financial information.

Part II.A. of the Release accompanying the Proposed Standard discusses the engagements for which an engagement quality review is required. The Release states that, in addition to audit engagements performed in accordance with the standards of the PCAOB, the Proposed Standard also would apply to "other audit and attestation engagements" performed in accordance with the Board's standards. Paragraph 1 of the Proposed Standard states that the engagement quality review would be required for "each engagement" performed and completed in accordance with PCAOB standards. In our view, it is unclear whether the Board intends the review to apply to all attestation engagements performed for issuers (e.g., agreed-upon procedures reports) or only those for which a report would be filed with the SEC, such as reports required under Regulation AB. We believe that further clarification about the applicability of the proposed engagement quality review requirement would be helpful.

In any event, we believe that a requirement to apply an auditing standard on engagement quality review to an engagement otherwise performed in accordance with attestation, not auditing, standards would result in confusion and inconsistent practice. Accordingly, we believe any engagement quality review requirement for attestation engagements should be provided for separately in the attestation standards rather than the auditing standards.

Views Relating to the Proposed Effective Date

We are concerned that the proposed effective date for reports issued on or after December 15, 2008 will not permit sufficient lead time for audit firms to re-evaluate the engagement quality reviewer assignments under the Proposed Standard. Engagement quality reviewer assignments typically are made at the beginning of the annual audit cycle so the assigned reviewer can participate in audit planning activities and timely reviews of interim financial information. Assignment of a different engagement quality reviewer later in the 2008 audit cycle could cause inefficiencies and might detract from the effectiveness of the reviews. We recommend that the effective date of the final standard be for audits and interim reviews of periods beginning on or after December 15, 2008.

* * * * *

We would be pleased to discuss our comments with members of the Public Company Accounting Oversight Board or its staff.

Very truly yours,

Ernst & Young LLP



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May 5, 2008

Office of the Secretary, PCAOB
1666 K Street, NW
Washington, D.C. 20006-2803

Via email: comments@pcaobus.org

Re: PCAOB Proposed Auditing Standard – *Engagement Quality Review and Conforming Amendment to the Board's Interim Quality Control Standards*

Dear Sir:

The Accounting Principles and Auditing Standards Committee (the “Committee”) of the Florida Institute of Certified Public Accountants (“FICPA”) has reviewed and discussed the subject Proposed Auditing Standard (the “Standard”), including the eleven discussion questions contained therein, and has the following comments:

Question # 1

The Committee believes that the Standard quite clearly proposes broad guidelines as to the function of the concurrent reviewer. In addition, the Standard enhances the firm’s quality controls over various stages of the audit engagement. The lack of a stated objective allows a certain degree of professional judgment depending on the size and complexity of the engagement.

Question # 2

The Committee concurs that, to be consistent, all engagements subject to the standards of the PCAOB should be subject to the Standard’s quality review procedures. Exceptions could lead to possible oversights in the application of this Standard.

Question # 3

The Committee concurs that the Standard is very accurate in its mandated requirements of the engagement quality reviewer. It is of significant importance in this Standard that the qualifications of the quality reviewer be similar to the requirements of ISQC No. 1.

Question # 4

The Committee believes that the timing of the consultation at key stages of the audit engagement would meet a twofold function: evaluating the engagement planning and identification of significant risks when timing is important and remedial actions can be implemented.

Question # 5

The Committee believes that the scope and extent of engagement quality review procedures are appropriate in the context that it allows the audit engagement team to exercise discretionary professional judgment in lieu of a boilerplate checklist approach. The broad concept of the concurrent reviewer function is well established by the general expectations attributed to it in the body of the Standard.

Office of the Secretary, PCAOB
May 5, 2008
Page 2

Question # 6

The Committee feels that the risk-based approach proposed by the Standard will only be truly effective if the quality control procedures are in conjunction with engagement planning review and consulting during various stages of completion of the engagement.

Question # 7

The Committee concurs with the proposed requirements for the review of the engagement team's documentation in that the reviewer must evaluate, for those areas reviewed, whether this documentation supports the conclusions reached, indicates that the engagement team responded appropriately to matters that present significant risks and meets the documentation requirements of Auditing Standard No. 3.

Question # 8

The Committee concurs with the timing of the review as long it provides sufficient time to implement remedial actions for the resolution of auditing and accounting issues raised during this review.

Question # 9

The Committee concurs that the reviewer's concurrent approval of the issuance will discourage the release of financial statements before all significant matters are resolved. This added approval will safeguard against the issuer's undue pressure on the engagement partner.

Question # 10

The Committee feels that the documentation requirements for the engagement quality review are adequate.

Question # 11

The Committee feels that all documentation pursuant to Auditing Standard No. 3 should be consistently applied as it relates to the concurrent review. This is based on the premise that any resulting remedial procedures and adjustments have become part of the required documentation of the engagement.

The Committee appreciates this opportunity to express its views on the subject Proposed Auditing Standard. Members of the Committee are available to discuss any aspects of this response.

Respectfully submitted,

Yanick J. Michel

Yanick J. Michel, CPA, Chair
FICPA Accounting Principles and Auditing Standards Committee

Committee members coordinating this response:

Richard G. Edsall, CPA
Joel S. Baum, CPA



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May 9, 2008

Public Company Accounting Oversight Board
Attention: Office of the Secretary
1666 K Street, N.W.
Washington, D.C. 20006-2803

RE: Rulemaking Docket Matter No. 025
Proposed Auditing Standard – Engagement Quality Review

Members of the Board,

I appreciate the opportunity to submit my comments to the Board with respect to the proposed auditing standard on engagement quality review. I retired from public accounting in 2007 after 27 years at Deloitte & Touche LLP and am currently a full-time faculty member at the University of Notre Dame teaching undergraduate and graduate courses in accounting and auditing.

My comments are as follows:

Question 1: I believe the standard should include an overall objective. Such objective should be consistent with the Board's goal of continually improving the quality of audits of public companies by ensuring registered public accounting firms have appropriate procedures in place to help provide those firms with reasonable assurance that their professionals are complying with PCAOB standards.

Question 2: I believe that an engagement quality review should be performed on all engagements conducted in accordance with PCAOB standards. I further believe that the engagement quality review standard should leave no doubt that such is the case. In particular, while the standard does state "engagements performed and completed in accordance with the standards" of the PCAOB in its very first paragraph, the tone of the standard is such that it appears to relate only to attest engagements related to financial statements and management's assertions regarding internal control. The quality review should apply to all deliverables provided to public company clients in accordance with PCAOB standards including management letters, communications with audit committees (both formal and informal), letters to underwriters, engagement letters and communications with other auditors. I believe the Board is committed to ensuring a culture of quality pervades all facets of the profession and the quality review process should be integral to that culture.

Question 3: While I appreciate the staffing issues of small registered public accounting firms, I have concerns about the provisions for quality reviews being performed by employees or others who are not at a level of authority in the firm comparable to the individual with final authority for the engagement. Apart from the potential human resource ramifications of subordinates being placed in the position of potentially exercising "veto power" over the engagement team, I am concerned such employees would not meet the standard's criteria of having the skills to perform in the role of the individual with final authority over the engagement being reviewed. An audit manager, for example, would likely not have the experience or judgment necessary to function as a signing partner for the audit of a registrant otherwise that individual would already be a

partner and have responsibility for his or her own engagements. If the Board believes this is appropriate, it should consider the need to ensure that employees placed in the quality reviewer position have the freedom within their organizations to perform this function without fear of adverse repercussions and should reconsider the requirement that the quality reviewer have the requisite skills to function as the individual with final authority for an engagement of the size and complexity as the engagement being reviewed.

Question 4: Having served as a quality reviewer for hundreds of engagements, I can state from experience that concurring reviewers regularly raise questions and provide comments to engagement teams that cause changes in audit approaches, conclusions and documentation. Just as there is no belief that auditors who propose adjustments to their clients as a result of errors detected in the course of an audit are no longer independent because they are performing “bookkeeping” for their clients, the standard should be clear that quality reviewers who correct, teach or otherwise cause changes to engagements to improve engagement quality in accordance with this standard have not acted in a manner that causes their objectivity to be impaired.

Question 5: The scope appears appropriately comprehensive. The Board may wish to consider providing guidance for those situations in which the quality reviewer is changed either during the course of the engagement or following the engagement. Successor quality reviewers may need to obtain the same working knowledge of the base engagement as their predecessor in order to provide the same quality review as the predecessor. For example, quality reviewers who assume that responsibility midway through an engagement would, of course, need the same level of knowledge as if they had been in that position from the beginning. However, a quality reviewer who must approve the reissuance of an audit report via consent for a former client’s filings with the SEC may not need the same level of knowledge as the quality reviewer who served in that capacity for the original filing. I believe this may also be a potential issue for small firms who will use quality reviewers outside their firms and may be faced with greater turnover in those individual quality reviewers than firms who have sufficient resources within. It may also adversely impact the willingness to serve in that capacity of those outside that small firm who are approached to be quality reviewers.

Question 6: The risk-based approach appears sufficient for the Board’s purposes.

Question 7: The requirements are appropriate; however the Board should consider specifying in paragraph 8 that the areas being reviewed specifically include the related documentation. While the Board does suggest that in paragraph 10, I believe specific reference in paragraph 8 would leave no doubt as to intentions of the standard. For example, 8.a. could read as follows: “Obtain and review the engagement team’s documentation of its understanding...” If it is the Board’s intent that the quality reviewer develop an independent understanding and compare that understanding to the engagement team’s documentation, I believe the Board should make that clear. Similarly, 8.c. could read “Review the engagement team’s documentation of its evaluation...” Again, if it is the Board’s intent that the quality reviewer perform an independent evaluation and compare that to the engagement team’s evaluation, I believe that should be stated.

Question 8: The specified timing is appropriate. The Board has left no doubt that engagements are not complete and conclusions cannot be delivered without the concurrence of the quality reviewer.

Question 9: The standard is appropriate; however I believe the perceived potential for “second guessing” may increase the exposure of prospective quality reviewers to a level that will make it more difficult for small firms who must obtain their quality review from individuals outside their firms to obtain those resources and thus continue as registered public accounting firms. While this potential should not take precedence over the Board’s goals in this area, the Board should consider any public policy issues that may be attendant on this possibility.

Question 10: The documentation requirements appear appropriate.

Question 11: For audits (including quarterly review procedures and audits of internal control), the required documentation of the quality review is clearly part of the documentation of the audit and is, therefore, subject to all the requirements of AS No. 3. Letters and reports that are incidental to those engagements (e.g., communications with audit committees) are likely also covered by AS No. 3. It is not clear that the Board has documentation standards explicitly related to other engagements subject to its standards (e.g., letters for underwriters). The Board may wish to consider the need to specify any particular documentation requirements it may have intended with respect to quality reviews of these other engagements.

Finally, I believe that the quality review process is a “second line of defense” in the area of engagement quality and the quality reviewer should not be portrayed as having joint and several responsibility with the individual having final authority for the engagement. Accordingly, I would encourage the Board to consider a project to address the qualifications and duties of the members of the engagement team – the “first line of defense” – with respect to engagement conduct and quality.

I appreciate the opportunity to offer my comments.

Sincerely,

s/ James L. Fuehrmeyer, Jr.

James L. Fuehrmeyer, Jr. MBA, CPA
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Department of Accountancy
University of Notre Dame
Notre Dame, IN 46556-5646

From: Jeffrey Gilbert [mailto:jsgcpa@pacbell.net]
Sent: Thursday, May 08, 2008 11:52 PM
To: Comments
Subject: Engagement Quality Review Standard Proposed

Request is made to extend the effective date of the Engagement Quality Review Standard so that Firms like mine have more time to reformat themselves to meet the requirements of the proposed standard. I propose a one-year extension to November 15, 2009, which would allow me to perform audits under the current rules through the 2008/early2009 audit period to satisfy engagements of I have been contracted to perform. I am a sole practitioner who is currently is not required to have a concurring partner review because I was not a member of the AICPA SEC practice section in 2003 when I became a member of the PCAOB.

The November 15, 2008 effective date is just not enough time to allow me to maintain the level of audit services while attempting to engage a reviewer or merge with a Firm that would allow me to satisfy the objectives of the proposed standard. Basically my current method of operations will be obsoleted by this new standard.

Thank you,

Jeffrey S. Gilbert

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May 12, 2008

Office of the Secretary
Public Company Accounting Oversight Board
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Via e-mail: comments@pcaobus.org

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Re: PCAOB Rulemaking Docket Matter No. 025, *Engagement Quality Review*

Dear Board Members and Staff,

We appreciate the opportunity to comment on the proposed auditing standard, *Engagement Quality Review*. We support the Public Company Accounting Oversight Board's ("Board" or "PCAOB") mission to develop auditing standards that promote audit quality, and we believe that a robust and effective engagement quality review enhances audit quality. In our opinion, an objective engagement quality review that focuses on a review of significant matters, including significant judgments made and conclusions reached by the engagement team, will accomplish that purpose. We believe that the proposed standard does not clearly articulate the objectives of the quality review and that the proposed requirements will result in additional audit time and costs that will not have a commensurate benefit to audit quality.

Objective of the engagement

We believe that a carefully crafted objective would enable the engagement quality reviewer to know when he or she has fulfilled the objective of the standard. The objective would also help define who would be qualified to perform an engagement quality review in that the person qualified to perform the review would need to have the skills to meet the objective. The objective also would clarify expectations of third parties, for example, financial statement users and regulators, with respect to what an engagement quality review is and is not.

We believe that an objective based on the existing standard is appropriate. We suggest:

The objective of the engagement quality reviewer is:

- a To review the documentation of those significant auditing, accounting, and financial reporting matters, including significant judgments made and conclusions reached by the engagement team as a result of the procedures performed.

- b On the basis of the review of audit documentation and discussions with the engagement team, to conclude whether matters that have come to his or her attention would cause the engagement quality control reviewer to believe that the audit was not performed in accordance with the standards of the PCAOB or that the financial statements are not in conformity with generally accepted accounting principles.

We believe it is important that the objective maintain the separation between the engagement partner and the engagement quality reviewer. That is, the objective should reflect that the requirement is to review significant matters, and not to perform a separate audit risk assessment or substantive procedures to obtain audit evidence.

The engagement quality review process

We have concerns that the proposed standard fundamentally changes the role of the engagement quality reviewer. Our first concern is with the “knows or should know” standard. We believe that the engagement quality reviewer will have to perform substantial work before being comfortable that he or she knows everything that he or she *should* know – especially since what should have been known will inevitably be judged with hindsight.

The concern is exacerbated by the lack of boundaries around some of the procedures that the engagement quality reviewer is required to perform. For example, paragraphs 8(a) and 8(b) require the engagement quality reviewer to obtain an understanding of the firm’s recent engagement experience with the company, risks identified in connection with the firm’s client acceptance and retention process, the company’s business, significant activities, and significant reporting issues and risks. The proposal, as drafted, appears to require the engagement quality reviewer to obtain his or her own understanding, rather than to obtain such an understanding through inquiries of the engagement team and the review of the audit documentation.

Paragraph 8(c) requires the engagement quality reviewer to review the engagement team’s evaluation of the firm’s independence in relation to the engagement. We note that engagement teams rely on the firm’s systems in this area. We believe that the engagement quality reviewer’s review should be limited to the engagement team’s evaluation of threats to independence and safeguards put in place to protect against those threats. The review also should cover the engagement team’s required communications with the audit committee concerning independence.

We also believe that paragraph 9 requires an independent risk assessment by the engagement quality reviewer rather than a review of the engagement team’s risk assessment. We do not believe that an engagement quality reviewer can perform a risk assessment that is equivalent to that of the engagement team without incurring unnecessary costs, since such a risk assessment would be duplicative.

We believe that the requirement in paragraph 10 to “evaluate whether the engagement documentation of the *matters* that were subject to the engagement quality review procedures... is consistent with the requirements of PCAOB Auditing Standard No. 3”, goes beyond what should be required of the engagement quality reviewer. First, it is the responsibility of the

engagement partner to determine that the engagement documentation is consistent with the requirements of Auditing Standard No. (AS) 3. Second, the entire engagement is “subject to the engagement quality review procedures.” Finally, the documentation associated with any particular *matter* might be quite voluminous. We question how far the engagement quality reviewer would have to look for missing documentation. If the requirement remains, we believe that it should be to evaluate whether the documentation that the engagement quality reviewer has reviewed is consistent with the requirements of PCAOB AS 3.

We believe that the extent of these requirements, when considered in conjunction with the statement in paragraph 12 that “[t]he engagement quality reviewer must not provide concurring approval of issuance if he or she *knows, or should know* based on the requirements of the standard...”, means that the engagement quality reviewer must obtain a level of knowledge to be able to provide assurance at a level comparable to that of the engagement partner (and in some cases, for example, in the case of a review of interim financial information, greater than the engagement partner). We believe that the additional communication between the engagement quality reviewer and the company that would be necessary for the engagement quality reviewer to obtain this level of knowledge will make it difficult for the engagement quality reviewer to perform the review without conflicting with the requirement to maintain objectivity, as set out in paragraphs 5-6. This will add significant cost and may raise concerns about the ability of the engagement quality reviewer to maintain his or her objectivity.

Notwithstanding the PCAOB’s stated beliefs that the proposal should not have a radical effect on the basic nature of reviews or on the cost of public company auditing, we believe that, if adopted as proposed, this standard will fundamentally change the nature of engagement quality reviews. We believe it will impose substantial unnecessary additional costs on public company audits, and increase the time needed to perform the engagement quality review such that it may significantly affect the ability of accelerated filers to make timely filings with the U.S. Securities and Exchange Commission (“SEC”).

We believe that an engagement quality reviewer who performs the review using due professional care and appropriate professional judgment would have an adequate basis to determine if something came to his or her attention to indicate that one of the four conditions in paragraph 12 exists. PCAOB Rule 3502, *Responsibility Not to Knowingly or Recklessly Contribute to Violations*, would appear to address this issue. To avoid the unintended consequence of engagement quality reviewers spending inordinate amounts of time searching for what they “should know,” we suggest that the PCAOB rely on the concepts of due professional care, professional judgment, and lack of recklessness that already exist in the literature.

Engagements for which an engagement quality review is required

We commend the PCAOB for the proposal to require that all registered public accounting firms – not just those that were members of the American Institute of Certified Public Accountant’s SEC Practice Section in April 2003 – be required to comply with the final standard. We believe that this certainly is in the public interest.

We note that the proposed standard would apply to all engagements performed in accordance with the standards of the PCAOB. We recommend that the applicability of the requirements, and of the standard itself, to engagements other than audits, for example, attestation engagements, letters for underwriters, reports on the application of accounting principles, and interim reviews, be carefully considered. While it may be appropriate to require an engagement quality review for these other engagements, we found that the requirements in this proposal were so specifically tailored to audits, that it would be difficult to apply the proposed standard to these other types of engagements. For example:

- We do not believe that it would be necessary for the engagement quality reviewer to obtain an understanding of significant financial reporting issues and risks (paragraph 8(b)) when reviewing an attestation engagement on the assessment of compliance with servicing criteria under the SEC's Regulation AB, *Asset-Backed Securities*.
- There is misunderstanding and disagreement on the period of time that the "prior period" (paragraph 8(g)) covers in the case of a third-quarter review of interim financial information or a report on the application of accounting principles. Some believe it is the previous quarter. Others believe it is the prior year's audited financial statements.
- We do not believe that it would be necessary for the engagement quality reviewer to read other information in documents containing an attestation report on the assessment of compliance with servicing criteria under the SEC's Regulation AB (paragraph 8(h)), in those circumstances where the practitioner performing the attestation engagement is not required to read such information.
- Paragraph 9 requires the engagement quality reviewer to assess whether there are areas that pose a higher risk that the engagement team has failed to obtain "sufficient competent evidence." In the case of a review of interim financial information or letters for underwriters, "sufficient competent evidence" goes beyond the evidence that the engagement team would be required to obtain.
- Paragraph 10(a) implies that the requirements of AS 3 now apply to attest engagements, which goes beyond the stated scope of AS 3.

Furthermore, in the case of a review of interim financial information, it appears that the proposed standard puts the engagement quality reviewer in the position of having to obtain more evidence, and a higher level of assurance, than the engagement team. For example:

- An engagement team's documentation in a review ordinarily does not include explicit risk assessments (paragraph 8(d) and paragraph 10).
- A review does not ordinarily contemplate obtaining "sufficient competent evidence" (paragraph 9 and 12).
- In a review, the affirmative conclusion that the engagement quality reviewer must reach in paragraph 12 goes beyond the negative assurance required of the engagement team.

We believe that, in order to maintain the specificity in this proposed standard, it would be helpful to keep it focused on audits of financial statements, and at some time in the future, draft other standards that apply to other types of engagements. This approach would have the added benefit of keeping the auditing standards and the attestation standards clearly delineated.

Qualifications of the engagement quality reviewer

We agree with the proposal to allow an engagement quality reviewer to be a partner of the firm, another individual in the firm, or an individual outside the firm. We believe that this is important to smaller registered firms, and will allow the firms to appoint appropriate engagement quality reviewers while also helping to alleviate some of the challenges associated with work compression, the five-year rotation requirement, and the limited number of available qualified resources. We also fully support the provision that an engagement quality reviewer should be an associated person of a registered public accounting firm, and that he or she should have competence, independence, integrity and objectivity.

With respect to the description of what constitutes a competent engagement quality reviewer, we note an apparent inconsistency between the proposal in paragraph 2, which allows the engagement quality reviewer to be another individual in the firm, and the requirement in paragraph 4 that the engagement quality reviewer possess the level of knowledge and competence relating to accounting, auditing, and financial or other reporting required *to serve as the person who has the overall responsibility for the same type of engagement*. We read the emphasized phrase to mean that a competent senior manager would not be qualified to serve as the engagement quality reviewer since this person was not a partner. In addition, the portion of this phrase that states “for the same type of engagement” indicates that, if the reviewer had not been a person with overall responsibility for an engagement of the same size, complexity, etc., then that person could not qualify as an engagement quality reviewer, even if that person were a partner.

Assuming that an objective of the proposed standard is developed, we believe that the following edit to paragraph 4 would help (1) eliminate this apparent inconsistency, and (2) properly cast the skills necessary to perform the engagement quality review as those technical skills necessary to perform the review, and not necessarily all of the skills required to be an engagement partner:

The engagement quality reviewer must possess the level of **technical** knowledge and competence relating to accounting, auditing and financial or other reporting required to **fulfill the objective of this standard** ~~serve as the person who has overall responsibility for the same type of engagement.~~

Footnote 18 of the release states that, “The determination of what constitutes the appropriate level of **technical** knowledge and competence should be based on the circumstances of the engagement, including the size or complexity of the business.” We believe that this would be helpful guidance to be included in the body of the standard, perhaps as a note to paragraph 4.

Concurring approval of issuance

The proposed standard requires the engagement quality reviewer to provide concurring approval of issuance of each audit report, and that such approval cannot be granted if certain conditions are present. On page 16 of the release, it is acknowledged that differences of opinion could occur between the engagement team and the engagement quality reviewer, and that, if those differences have not been satisfactorily resolved, the engagement quality reviewer must not provide concurring approval. We believe that this resolution of differences is an important contributor to audit quality, but the concept is not addressed in the proposed standard. We suggest that the standard state that, if one of the four conditions in paragraph 12 exists, *and those differences have not been satisfactorily resolved*, the engagement quality reviewer must not provide concurring approval.

Documentation of an engagement quality review

We believe that some of the requirements in paragraph 14 are not clear, or go beyond existing documentation requirements. For example:

- Paragraph 14(b) requires documentation of the *areas* of the engagement *subject to the* engagement quality review. Since all areas are subject to the engagement quality review, this requirement is not clear. If the Board means that the areas reviewed by the engagement quality reviewer should be documented, that should be clarified. Even then, how, and to what level of detail, one documents an “area” is not clear.
- Paragraph 14(d) requires the documentation of when the procedures were performed. An engagement quality review involves a variety of procedures, including review of individual work papers, review of draft financial statements and SEC filings, and discussion with the engagement partner and other engagement team members. The requirement to document when each of these procedures was performed would be a higher standard for the documentation of engagement quality reviews than for the engagement team. Compliance with this requirement will result in multiple signoff dates for each procedure performed.
- Paragraph 14(e) requires the documentation of the results of the review procedures. We believe that this could be read as requiring a detailed record of procedures performed and considerations made by the engagement quality reviewer, questions asked of the engagement team (e.g., review notes) with documentation of the engagement team’s responses, etc. This would result in a significant change in practice, without an improvement in audit quality.

We recommend that the Board eliminate paragraph 14(e), since the results of the review procedures will be clear when the engagement quality reviewer concurs with the issuance of the report. We further recommend that the documentation requirements in this standard parallel the documentation requirements in paragraph 6 of AS 3, as follows:

Documentation of an engagement quality review must contain sufficient information to enable an experienced auditor, having no previous connection with the engagement:

- a To understand the nature, timing, extent and results of the review procedures performed, and conclusions reached, and

b To determine who performed the review procedures and the date such review procedures were completed.

Tone at the top

The proposed standard does not include a discussion of the importance of the firm's tone at the top in ensuring the objectivity and independence of the engagement quality reviewer. This matter is included in the interim standards and should not be omitted.

Engagement partner movement to engagement quality reviewer

The Board's interim standards state, "... a prior audit engagement partner should not serve as the concurring partner reviewer for at least two annual audits following his or her last year as the audit engagement partner." We believe that this requirement is appropriate and should be retained in the final standard.

Paragraph-level comments

The following offers paragraph-level comments for your consideration.

Paragraph	Comment
3	The note to this paragraph deals with a matter that is a component of a firm's quality control system and therefore, it is not appropriate to include it in an auditing standard.
5	The proposal indicates that the engagement quality reviewer may seek assistance from others to complete the review, but the overall responsibility remains with the engagement quality reviewer. We believe it would be appropriate to indicate that those who assist the engagement quality reviewer also must be independent, have integrity, maintain objectivity <i>and be competent</i> .
6	Paragraph 6 appears to prohibit communications between the engagement quality reviewer and management or those charged with governance. We recommend that the standard adopt language that is in Footnote 3 of the PCAOB's interim standard on concurring reviews: "It is not unusual for clients to be aware of the existence of a concurring partner reviewer. A client may contact the concurring partner reviewer with respect to matters requiring immediate attention when the audit engagement partner is not available because of illness, extended travel or other reasons. When a concurring partner reviewer is thus required to deal with an accounting, auditing or financial reporting matter, he or she should advise the audit engagement partner of the facts and circumstances so that the audit engagement partner can review the matter and take full responsibility for its resolution."
8(i)	"Appropriate" communication, particularly with management, occurs throughout the course of the audit, is often verbal, and usually not in the presence of the engagement quality reviewer. We believe that the engagement quality reviewer should review whether specific communications, for example, those regarding audit adjustments and control deficiencies, are appropriately documented.
9	The proposed standard requires the engagement quality reviewer to assess whether there are areas within the engagement that pose a "higher risk" that the engagement team has failed to obtain sufficient competent evidence or reached an inappropriate conclusion. This seems to focus the risk on the engagement team, and not on the risk of material misstatement of the financial statements. We believe that it would be more effective to consider areas of significant risk of material misstatement of the financial statements, and whether the engagement team appropriately addressed them. Otherwise, there is a risk that the engagement quality reviewer may focus on areas where there is a higher risk that the engagement team has failed to obtain sufficient competent evidence or reached an inappropriate conclusion, but in an area where there is not a significant risk of material misstatement of the financial statements.

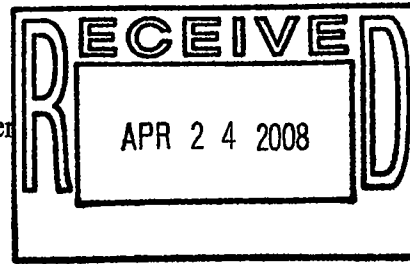
We would be pleased to discuss any of our comments with you. If you have any questions, please contact Mr. John L. Archambault, Managing Partner of Professional Standards, at (312) 602-8701.

Sincerely,



Grant Thornton LLP

James H. Hance, Jr.
Bank of America Corporate Center
NC1-007-52-17
100 North Tryon Street
Charlotte, NC 28255



April 21, 2008

Office of the Secretary
PCAOB
1666 K Street
Washington, DC 20006-2803

Gentlemen:

I am providing a comment letter to you on your Proposed Auditing Standard No. 7, *Engagement Quality Review*.

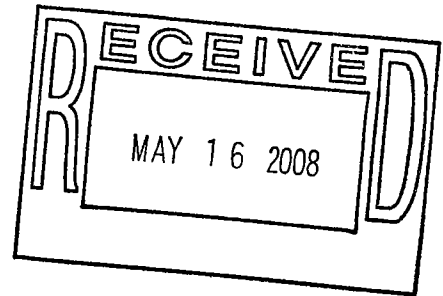
Very simply, I think that what is proposed in this standard would be an additional burden to audit committees and companies with very little return. The Proposal clearly shows that added auditing effort would result. Since the advent of Sarbanes-Oxley, audits appear to be working well and additional burdens are not needed at this time.

I chair an audit committee and have seen first-hand cost versus benefit of a number of the proposed auditing standards, and in my judgment going from a negative assurance by a concurring partner to positive assurances is not beneficial.

Sincerely yours,

James H. Hance, Jr.

May 8, 2008



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

RE: Rulemaking Docket 025: Proposed Auditing Standard – Engagement Quality
Review and Conforming Amendment to the Board’s Interim Quality Control Standards

Dear Gentlemen:

HealthSouth Corporation appreciates the opportunity to comment on the proposed auditing standard – *Engagement Quality Review and Conforming Amendment to the Board’s Interim Quality Control Standards*. We share the Board’s view that a well-performed engagement quality reviews are an important element in establishing a basis for the investor reliance on audits. However, we are concerned the proposed standard will result in additional effort and resulting fees that do not correspond into additional audit quality.

Also, the Sarbanes-Oxley Act of 2002 required each registered public accounting firm to provide a concurring or second partner review and approval of each audit. The Board adopted, on an interim basis, the SEC Practice Section’s requirement for concurring reviews. The proposed standard’s requirements exceed the SEC’s standard and also exceed the proposed redrafted international standards. The additional requirements and resulting cost do not appear to provide significant benefits or additional audit quality that outweigh the resulting increased cost to registrants and to the investor community.

We appreciate the opportunity to express our views on the proposed auditing standard.

Sincerely,

A handwritten signature in black ink, appearing to read "E. Blechschmidt".

Edward A. Blechschmidt
Chairman of the Audit Committee
HealthSouth Corporation



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April 29th, 2008

To: Office of the Secretary, Public Company Accounting Oversight Board

Re: Horwath International's comments on PCAOB's Rule Making Docket Matter No. 025- Engagement Quality Review

We applaud the Board's efforts to enhance the quality of the auditing standards for audits of US public entities. We have seen the 2nd partner/reviewer process evolve since its inception in the 1980's and believe it to be a meaningful and necessary procedure which provides some added assurance about specific engagement performance and the functionality of a firm's quality control process at the engagement level.

We understand the PCAOB's objectives to make the engagement quality review process more consistent and effective within firms and between firms, and, to address such reviews done in small audit firm environments. Our comments and observations are embedded in our responses to the question section of the release below.

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?

*We believe an objective would be useful for several reasons. To quote the Board's language on page 14 of the draft (in a discussion of audit documentation) "...quality audit documentation is a record of the actual work performed, which provides assurance that the auditor accomplished the **planned objectives**. (our emphasis). Without stated objectives the purpose of the review will be viewed very differently by firms and by reviewers themselves. Many will consider the review to require the reviewer to provide in depth review of the work in many areas as they might do as a principal reviewer thereby losing perspective in the process. Objectives would help focus the review and help define the reviews purpose to others outside the audit firm.*

We believe a general purpose statement describing the purpose of the review, its scope and the limitations of the review, and, the importance of using professional judgment in evaluating what to review. Also the objective should include a statement that the review does not relieve the engagement partner/director from the final responsibility for the firm's report(s).

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 required?

We believe that the involvement in AU Sec 711 procedures (specifically with respect to the use of the auditor's report) by an engagement quality reviewer for an issuer undertaking a filing under the Securities Act of 1933 is a natural extension of the quality review process. The involvement of an engagement quality reviewer for SAS 100 reviews for interim filings is a cost/ benefit consideration. We believe the costs and the logistics of an engagement quality review for this purpose is tenuous at best, although notification by an engagement partner of significant matters encountered in SAS 100 reviews to an engagement quality reviewer who may later be involved in the annual audit would be beneficial.

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

Yes, we believe the level of qualification as related to the competencies of the engagement partner is generally an appropriate benchmark. However, we note the discussion in the introduction on page 9 which drives to industry competency. We believe small firms with public company audits may be significantly handicapped being able to obtain outside quality control reviewers with competencies in specialized industries, since specialized industries tend to have a smaller cadre of servicing firms. If an experienced auditor/ reviewer attends relevant training courses and seeks assistance from other individuals to supplement his or her skill levels when necessary, this individual should be able to provide the quality review for such a firm.

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

Consultations should be permitted since they provide insights into appropriate solutions. If the reviewer is objective and is not sure of his or her response, then the appropriate firm or other resource will be called on. It's the same as the client consulting on the auditor with an issue. The reviewer should be advised not to initiate the solution as that would bias the review.

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

Yes. We think the level and description of recommended procedures is appropriate and the discussion incorporating risk is supportive of the review's objectives.

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 standard be changed?

Not entirely, we think that the risk based approach to audit results (response, conclusions, and documentation) is fine; however, the question posed is the sufficiency of problem identification. It is our experience that problem identification in financial statement audits is best addressed in the planning phase. For this purpose we will define planning to include all processes through the preparation of the audit plan. We think it would be appropriate to provide guidance in this section (paragraph 9) which references to paragraph 11 timing of the review. We believe in high risk engagements (overall risk) that the quality reviewer look at planning documents before the further audit procedures are completed. If problems are identified during this phase of the engagement then more time and effort can be spent more effectively by engagement personnel. Perhaps these two paragraphs can be combined with planning emphasis in the quality review for high risk engagements.

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

We think the proposed standard in the area is fine for now. As auditor’s become more proficient in documenting their work under AS-3 a firm’s own review process will be able to address deficient documentation and this part of the proposed standard may be able to be reduced at some future date due to redundancy of this procedure.

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

See Question 6 above.

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

*No. We found this to be the most problematic issue in the proposed standard. We agree with the matters that are the basis for the reviewer’s conclusion. We do not agree with the language that the reviewer cannot approve if he or she **should have known** (our emphasis) about deficiencies in the basic audit requirements. “Should have known” is included in definitions of simple negligence. How does one evaluate what they should have known? By signing the approval if anything goes awry the reviewer is negligent. It seems that this standard would exceed the professional standards that the engagement partner is held to. We do not believe this approval, under this language, to be better than the limited or the negative assurance being provided under the existing standard. If a reviewer knows of an unresolved significant issue then he or she cannot approve the report(s). If “should have known” relates to any undetected issue it’s very problematical.*

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

The items included in paragraph 14 of appendix 1 in the proposed standard are sufficient to document the nature timing and extent of the procedures performed. It will be difficult for a reviewer to document situations where detail review was done for certain

subsidiaries in several accounts or financial transaction cycles and not in other similar subsidiaries, perhaps, just as a sampling procedure.

We believe that in many cases the focus of the review would be changed based on the assessment of the competencies and experience of the engagement team and of its supervision. A likely situation might be where the reviewer ran into several issues that were unacceptable or were marginally acceptable, in that case as in an audit, the reviewer would have several alternatives, including stopping the review, or expanding the review to ascertain the existence of other problematic matters, and their cause. The third bullet – documenting the procedures performed by the reviewer would then become a more sensitized matter. The level of documentation or its content would likewise become sensitized and raise the level of skepticism amongst others including post issuance and outside reviewers.

The question that needs to be addressed is the level of detail that is needed. We believe the level of detail should be sufficient to understand that other procedures were required by the reviewer and what transpired (file revision, expansion of procedures, firm consultation, etc). We suggest some guidance be placed in this section of the proposed standard.

If a significant overlay of documentation extends to the quality control review, we believe it would exceed documentation requirements specific to the review process performed by engagement partners/directors.

*Some of the most effective review we have experienced is what is not in the work papers and financial statements but what **should be** in them (our emphasis). The documentation follows the result.*

Question 11 – Should the proposed standard require documentation of the engagement quality review with other provisions contained in AS-3? If so which provisions should be applicable?

The proposed standard requires that AS-3 provisions related to subsequent changes and file retention be followed. We think these requirements are a suitable reminder. Significant issues that arise from the review will of necessity be incorporated in the significant issues documentation requirement or in other documentation that fall under AS-3.

Thank you for your kind attention.

Very truly yours

Julian E. Jacoby

Kamel W. AbouChacra

Julian E. Jacoby, Accounting and Assurance Director

Kamel W. AbouChacra, Associates Accounting and Assurance Director



Office of the Secretary
 PCAOB
 1666K Street N.W.
 Washington D.C. 20006-2803
 USA

By E-mail: comments@pcaobus.org

May 12, 2008

Dear Sir(s):

**Re.: 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**

The Institut der Wirtschaftsprüfer in Deutschland [Institute of Public Auditors in Germany], the professional organization representing public auditors in Germany, appreciates the opportunity to comment on the above-mentioned Proposed Auditing Standard – Engagement Quality Review and Conforming Amendment to the Board’s Interim Quality Control Standards (hereinafter referred to as the “proposed PCAOB auditing standard” or “proposed standard”).

We share the Board’s view that well-performed engagement quality control reviews are an important element in establishing a basis for investor reliance on audits and agree with the aims of the proposed PCAOB auditing standard. Subject to the issues raised below, we support the content of the proposed standard. We discuss our major concerns in detail below. In the Appendix to this letter, we respond to the questions posed by the Board and comment on the proposed effective date.

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GESCHÄFTSFÜHRENDER VORSTAND:
 Prof. Dr. Klaus-Peter Naumann,
 WP StB, Sprecher des Vorstands;
 Dr. Klaus-Peter Feld, WP StB CPA;
 Manfred Hamannt, RA



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Major concerns

The extent of engagement quality review procedures

We support the Board's statement on page 16 of the Release that the engagement quality reviewer's role is not to perform procedures amounting to a re-audit. We are, however, concerned that, contrary to this statement, certain requirements in paragraphs 8 and 9 of the proposed standard appear to require the engagement quality reviewer obtain an understanding of certain matters or knowledge, respectively, disproportionate to an engagement quality review. In this context, we refer to the Appendix to this letter in which we explain our concerns in relation to paragraphs 8 and 9 in more detail.

The source of an engagement quality reviewer's knowledge

In view of our comments relating to the extent of certain procedures required by paragraphs 8 and 9, we are concerned that the wording of the phrase "knows, or should know based on the requirements of this standard" in paragraph 12 may not be sufficiently clear. An engagement quality reviewer ought only be expected to know what he or she would reasonably be able to know as a result of having complied with the requirements of the proposed PCAOB auditing standard. It would be unreasonable and inappropriate for knowledge based on information gained with hindsight for example, to be included in this expectation. We therefore believe it is essential that the wording of paragraph 12 be unambiguous and also that each of the requirements of the proposed standard be worded such that they are not capable of misinterpretation.

We refer to the Appendix to this letter, in which we explain our concerns in respect of paragraph 12 in more detail.

Respective Authorities

The proposed standard does not clarify the respective responsibilities of the engagement partner and the engagement quality reviewer, nor does it stipulate how conflicting views between the engagement quality reviewer and the engagement partner are to be dealt with such that the firm will be in a position to grant permission to the client to use the engagement report.

According to our reading of paragraph 13, the engagement quality reviewer would assume a level of authority sufficient to block that of the engagement partner, because he or she can bind the firm by effectively vetoing the issuance



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of an engagement report. We are concerned that, given the different depth of knowledge that an engagement partner and an engagement quality reviewer can be expected to obtain, respectively in relation to the same engagement, it is not appropriate for the proposed standard to require the latter be able to block the engagement partner's authority without stipulating how such conflicts are to be resolved. The respective roles of an engagement quality reviewer and an engagement partner need to be clarified, such that the engagement partner's responsibility for the engagement is not diminished by the fact that an engagement quality review is performed.

In the Appendix to this letter we respond to question no. 9, further recommending that firms be required to establish procedures or measures to resolve any differences of opinion that may arise between the engagement partner and the engagement quality reviewer before a firm can issue an engagement report.

We would be very pleased to be of further assistance if you have any questions or comments about the content of our letter.

Yours truly,

Klaus-Peter Feld
Executive Director

Ulrich Schneiß
Director, Auditing

541/500

Enclosed: Appendix



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APPENDIX

Specific questions raised by the PCAOB in PCAOB Release No. 2008-002:

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?

We encourage the PCAOB to format its standards in a manner similar to that currently being adopted by the IAASB and the AICPA. Objectives are generally useful in focusing the public's expectation of what an auditor aims to achieve.

2. Should the 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 required?

Whilst the IAASB's equivalent standards require an engagement quality control review for audit engagements of listed entities, it is for the firm however, to establish a policy for determining which engagements other than audits of the financial statements of listed entities are to be subject to a quality control review. Criteria to consider when determining which engagements other than audits of financial statements of listed entities are to be subject to an engagement quality control review include, for example the nature of the engagement, including the extent to which it involves a matter of public interest or the identification of unusual circumstances or risks in an engagement or class of engagements. We suggest the PCAOB adopt a similar approach for engagements performed in accordance with PCAOB standards.

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

We support the proposal that suitably qualified persons both not necessarily at partner level and also external to the firm may perform engagement quality reviews. This allows more flexibility than current PCAOB's interim requirements, and is likely to be particularly helpful to smaller foreign registered firms seeking suitable engagement quality reviewers.

However, we note that the levels of knowledge and competence that an engagement quality reviewer must possess according to the proposed standard



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are more stringent than those stipulated in the PCAOB's interim requirements and by the IAASB in its counterpart standards¹. The proposals require the experience of the quality control reviewer to be sufficient to enable him or her to serve as engagement partner in the specialized industry (we refer to page 9 of the Release). This may be problematical for foreign audit firms, and in particular smaller firms, where the "pool" of potential engagement quality reviewers may be limited.

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?

We agree that consultation may certainly be useful at an early stage in the audit in some cases.

We support the proposal for consultation to be allowed, but at the same time, not so as to impair the engagement quality reviewer's objectivity. Nevertheless ultimate responsibility for the engagement should remain with the engagement partner.

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?

In our letter above, we have expressed concerns relating to specific paragraphs in the proposed standard. We comment further on these paragraphs as follows:

Paragraph 8:

As currently worded, subsections a and b of paragraph 8 requiring the engagement quality reviewer to "obtain an understanding of the firm's recent engagement experience with the company and risks identified in connection with the firm's client acceptance and retention process" and to "obtain an understanding of the company's business, significant activities during the current year, and significant financial reporting issues and risks", respectively may be interpreted to mean that the engagement quality reviewer should obtain the required under-

¹ [Proposed] ISQC 1 (Redrafted) paragraph A42 states that for an audit of a listed entity the engagement quality control reviewer "... would be an individual with sufficient and appropriate experience and authority to act as an audit engagement partner on audits of financial statements of listed entities."



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standings, essentially by repeating engagement procedures independently. We appreciate that the Board does not intend this to be the case, and therefore suggest the standard clarify that the procedures required do not extend beyond a review of the engagement documentation supplemented by discussions with the engagement partner and, as necessary, other engagement team members.

Similarly, paragraph 8f needs to clarify that the difficult or contentious matters referred to therein means only those significant difficult or contentious matters identified by the engagement team rather than implying any “new” matters are to be identified by the engagement quality reviewer.

We note that other procedures in paragraph 8 make specific or implied reference to the engagement team’s or the firm’s findings or actions, but this is not clearly the case in respect of sections a, b and f.

Paragraph 9:

In our view the requirement of paragraph 9 is likewise unclear. Paragraph 9 requires the engagement quality reviewer “based on the procedures performed in accordance with paragraphs 7 and 8, **and other relevant knowledge** possessed by the engagement quality reviewer” to “assess whether there are areas within the engagement that pose a higher risk that the engagement team has failed to obtain sufficient competent evidence or reached an inappropriate conclusion”. We interpret the phrase “other relevant knowledge” to mean that knowledge the engagement quality reviewer is required to possess in accordance with paragraph 4 of the proposed standard, rather than inferring a requirement for the engagement quality reviewer to obtain further relevant information to supplement that obtained by the engagement team. It would be helpful if the PCAOB were to clarify this in the text of the proposed standard, for example, along the lines of the following text currently specified in the interim requirements: “The concurring partner reviewer is not responsible for searching for additional matters to be considered by the engagement team. However, significant matters not previously identified by the engagement team that come to the concurring partner reviewer’s attention should be referred to and resolved by the engagement team with the concurrence of the concurring partner reviewer.”



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Paragraph 12:

We would like to suggest that the requirement of paragraph 12 be reworded to clarify that the phrase “knows or should know” contained therein is to be understood only in the context of the engagement quality reviewer having complied with the requirements of the proposed PCAOB auditing standard, i.e., excluding any additional facts or matters that become known with hindsight. Furthermore, performing all the procedures required by the proposed standard can give reasonable but not absolute assurance that the engagement quality reviewer will know everything that could become known in so doing. This also needs to be reflected, along the lines of “... he or she knows, or should reasonably be expected to know, that...”.

We comment further on the issue of final approval by the engagement quality reviewer prior to issuance of an engagement report in our response to question 9 below, because we believe paragraph 12 needs further amendment in this respect.

Finally, we also note that the requirement states that the “...engagement quality control review *must not* provide concurring approval ...”. We would like to point out that, logically and grammatically speaking, the negation of “must” in this case does not mean that the engagement quality control reviewer is prohibited from providing concurring approval, but that the engagement quality control review is not required to provide concurring approval. We believe that this is not what the PCAOB had in mind. For this reason, the words “must not provide” should be replaced with “may not provide” or “is prohibited from providing”.

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 refer to the detailed comments explaining our major concerns in the accompanying letter as well as the comments relating to paragraphs 8 and 9 above. We do not believe that all the procedures of paragraph 8 sufficiently reflect a risk-based approach.



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

We support a risk-based approach whereby the review of the engagement team's documentation does not extend beyond documentation of the matters subject to engagement quality review procedures.

Nevertheless, we believe that the requirements of paragraph 10a may not be practicable as regards the envisaged evaluation of consistency with the requirements of PCAOB AS-3. An engagement quality reviewer who only reviews selected parts of the engagement team's documentation may not be in a position to confirm that these parts are consistent with all the requirements of AS-3. For example, paragraph 5 of AS-3 requires in subsection a, that audit documentation "demonstrate that the engagement complied with the standards of the PCAOB"; unless a review of the complete documentation were performed this cannot be ascertained fully. In addition, unless the engagement quality reviewer were to re-audit, the engagement quality reviewer would potentially be unable to ascertain when the engagement team's documentation is incomplete. In such cases, evaluation of whether engagement documentation complies with paragraph 12 of AS-3 would likewise not be practicable.

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

In our opinion the flexibility as to timing of the engagement quality review envisaged in the proposed standard is appropriate.

We note the Board's belief (we refer to page 15 of the Release) that an engagement quality review "could be more effective if the review is performed shortly after the engagement team's resolution of significant issues", however, this may not be the case in all engagement circumstances. We would like to suggest the Board also recognize that in some engagements, particularly less complex or smaller companies, an engagement quality review performed towards the end of the engagement, as opposed to throughout that engagement, may also be effective.



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

In the attached letter, we have expressed concerns as to the respective authority of the engagement partner and the engagement quality reviewer, and also suggested the PCAOB introduce a requirement for firms to establish procedures to resolve any differences of opinion that may arise:

We note that the current interim requirements address both issues as follows:

Organizational Structure and Functions of the SEC Practice 1027 Section.39, APPENDIX E - Concurring Partner Review Requirement states: "The concurring partner reviewer's responsibility is not the equivalent of the audit engagement partner's responsibilities. Without first-hand knowledge of the client's business environment, the benefit of discussions with management and other client personnel, the opportunity to review client documents or controls, or the ability to observe the client's actions or attitudes, a concurring partner reviewer generally is not in a position to make the informed judgments on significant issues expected of an audit engagement partner." and "If the concurring partner reviewer and the audit engagement partner of the engagement have conflicting views regarding important matters, the disagreement should be resolved in accordance with applicable firm policy."

The international auditing standard ISA 220 also contains similar requirements and also requires the engagement partner not date the auditor's report until the completion of the engagement quality control review, thus clarifying that the engagement partner retains responsibility for the engagement:

[Proposed] ISA 220 (Redrafted), paragraphs 23 "The engagement partner shall remain responsible for the audit engagement and its performance, notwithstanding involvement of the engagement quality control reviewer." and 24 "Where differences of opinion arise within the engagement team, with those consulted or, where applicable, between the engagement partner and the engagement quality control reviewer, the engagement team shall follow the firm's procedures for dealing with and resolving differences of opinion."

In our opinion, similar requirements and statements need to be included in the proposed standard, such that the respective roles of engagement quality reviewer and engagement partner are clarified. It is important that the engage-



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ment partner retains full responsibility for the engagement and in no way relies on an engagement quality review as a safety net or corrective measure.

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

In our opinion, the documentation requirements are reasonable.

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?

No. We have not identified any further provisions that would be applicable.

The Board requests comment on the proposed effective date.

In our opinion, the proposed effective date is not appropriate, since until the SEC has given its approval to the proposed standard many engagements for which a report will be issued on or after December 15, 2008 may have advanced beyond their initial planning stages. Involvement of an engagement quality reviewer in accordance with the final version of this proposed standard at an early stage will no longer be possible. This is a particular problem for those firms not previously subject to the interim requirements or for which changes from those requirements may require adaptation of their previous practices.

In our opinion, a more reasonable approach would be to state that the auditing standard is applicable for fiscal years beginning on or after December 15, 2008.



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May 12, 2008

Office of the Secretary
Public Company Accounting Oversight Board
1666 K Street, N.W.
Washington, D.C. 20006-2803

PCAOB Rulemaking Docket Matter No. 025
Proposed Auditing Standard, *Engagement Quality Review*
and Conforming Amendment to the Board's Interim Quality Control Standards

Dear Mr. Secretary:

KPMG appreciates the opportunity to comment on the Public Company Accounting Oversight Board's (PCAOB or the Board) Release No. 2008-002 (the Release) that includes the Proposed Auditing Standard, *Engagement Quality Review*, and a Conforming Amendment to the Board's Interim Quality Control Standards (collectively, the Proposed Standard).

We would like to take this opportunity to formally recognize the significant effort of the Board and its staff in development of the Proposed Standard. We agree with the Board that a well-performed engagement quality review is an important element in establishing a basis for investor reliance on audits. We also agree with the Board's proposal that all registered public accounting firms be required to comply with the engagement quality review standard.

We do, however, have concerns regarding the fundamental change in nature and scope of an engagement quality review from what is described in the concurring review requirements in the Board's interim quality control standards and in international auditing standards.¹ We note increasing support for global convergence of auditing standards, and the Proposed Standard does not appear to be a step in that direction. In addition, the proposed change in nature and scope of an engagement quality review would result in significant incremental cost, and we do not believe that the increase in audit quality would be commensurate with the cost. We also are concerned about the lack of a stated objective of an engagement quality review. We believe it is critical that the Board provide greater clarity in the Proposed Standard, so that audit firms and engagement quality

¹ Proposed Redrafted ISA 220, *Quality Control for an Audit of Financial Statements*, was proposed by the International Auditing and Assurance Standards Board in July 2007 and is scheduled to be considered for adoption by the International Auditing and Assurance Standards Board in September 2008.



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reviewers have a clear understanding of what is expected in order to be able to properly fulfill their responsibilities. Our specific comments and recommendations regarding these and other concerns are provided in the remainder of this letter.

Overall Objective of the Proposed Standard

As noted on page 8 of the Release, the Proposed Standard does not include an overall objective of an engagement quality review. Furthermore, the objective is not implicit from the requirements in the Proposed Standard, particularly when considered in light of comments by Board members in the Board's February 26, 2008 open meeting. For example, one Board member stated that "the proposal should not have a radical effect on the basic nature of these reviews or on the cost of public company auditing." We would infer from this commentary that the objective of the Proposed Standard would be generally consistent with the objective in the Board's interim requirements.² However, as we will address more specifically later in this letter, we believe the Proposed Standard, if adopted as drafted, would fundamentally change the nature and extent (and cost) of engagement quality reviews. Further, another board member stated that "a thoughtful engagement quality reviewer – who after all has access to the same information we do as part of our inspections – could have found and focused the firm on these deficiencies [those identified by inspectors] before we inspected the firm," implying that the objective is to supplement or overlap with an inspection process (whether internal inspections as a part of a registered firm's quality control system or a PCAOB inspection), but on a real-time basis. We do not believe the objective of an engagement quality review should be the same as the objective of internal or external inspections. Inspections have distinct but different purposes and are generally conducted by teams of people, with fewer constraints on timing.

In our view, the objective set forth in the Board's current interim standard is an appropriate starting place for the overall purpose of the engagement quality review, and we propose including a similar objective in the engagement quality review standard. We recommend that the Board adopt the following objective for the standard:

The objective of the engagement quality review is to provide for an independent, objective review of significant auditing, accounting, and financial reporting matters including significant judgments made and conclusions reached that results in a conclusion about whether the engagement quality reviewer concurs with the issuance of an engagement report.

This language makes clear that the requirement is for a "review" of significant matters, not the performance of additional independent substantive procedures or evaluation of all aspects of the engagement team's work. It also serves to differentiate the function of the engagement quality reviewer from that of the engagement partner.

² The Board's interim requirement states that "the concurring partner review is an integral part of the firm's system of quality control and serves as an objective review of significant auditing, accounting, and financial reporting matters that come to the attention of the concurring partner reviewer and the resolution of such matters prior to the issuance of the firm's audit report with respect to financial statements"



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Page 3

Engagement Quality Review Process

The Proposed Standard

In light of our suggested objective, we are concerned about certain aspects of the Board's proposal. First, as further described below, we believe that the Proposed Standard goes well beyond the requirements of international auditing standards. Second, we believe that the proposed changes and additions to what is required by the Board's current interim standard (as well as by international auditing standards) will significantly alter the nature of an engagement quality review and result in additional costs that it will not provide a commensurate benefit to audit quality.

We believe that these concerns should be addressed by aligning the new standard with international standards, which we believe would create an appropriately focused and effective review standard. Moreover, doing so would be consistent with the growing demand for convergence of world-wide accounting and auditing standards and the recognition of the benefits of developing a single set of standards for world-wide use. We believe that further consideration should be given to the benefits of convergence and to avoiding the creation of unnecessary substantive differences in standards.

If, however, the Board does not believe convergence of this standard with international standards is appropriate, we urge the Board to, at minimum, consider and address the concerns about those provisions that differ significantly from international standards. We have recommended specific changes that we believe would appropriately support audit quality without the attendant costs of certain of the provisions in the Board's Proposed Standard. We believe that our recommended changes would result in a standard that is not only effective at meeting our proposed objective, but also one that can be implemented efficiently.

More specifically, and as more fully discussed below, we are concerned about the following incremental procedures in the proposal:

- A requirement that the engagement quality reviewer identify areas of "higher risk," not of material misstatement, but rather areas where, regardless of materiality, the engagement team might have failed to obtain sufficient competent evidence or might have reached an inappropriate conclusion (paragraph 9);
- A requirement that the engagement quality reviewer independently evaluate the adequacy of audit documentation, particularly its compliance with Auditing Standard No. 3, *Audit Documentation* (paragraph 10);
- Procedures that require the engagement quality reviewer to make "evaluations" or "determinations" that, without clarification, might be interpreted to require efforts similar to those required of the engagement team in performing the work itself, rather than a review of the engagement team's judgments and conclusions (paragraphs 7 and 8); and
- A new standard of performance for the engagement quality reviewer's work and a conclusion that departs from the negative assurance in the interim standard and, as proposed, requires an affirmative conclusion. The proposal would require the reviewer to affirmatively conclude that there is nothing the reviewer "knows or *should know*" that would preclude concurrence in the engagement team's issuance of the report (paragraph 12) (*italics added*).



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These provisions, taken together, would impose substantial new burdens on the engagement quality reviewer without a commensurate benefit to audit quality. As discussed above, the objective of the review should be to enhance audit quality by providing an independent, objective review of the significant accounting and auditing judgments and the conclusions reached. The Proposed Standard, however, would redirect the focus of the engagement quality reviewer away from the work of the engagement team to the work performed to carry out the reviewer's responsibilities. More specifically, in creating new standards of performance for the reviewer that require a "know or should know" level of assurance, these provisions become too focused on the adequacy of the engagement quality review itself, rather than on the quality of the work performed by the engagement team. For example, we believe that an engagement quality reviewer likely would interpret these provisions as a requirement for him or her to perform sufficient work to have a basis for separately forming his or her own independent determinations about such matters as whether appropriate consultations have taken place, whether appropriate matters have been communicated to the audit committee, whether there are areas that create a "higher risk" of non-compliance, and whether the engagement team complied with documentation standards. This may result in an engagement quality reviewer's perceived need to participate extensively in meetings with client management, to make his or her own inquiries of client personnel, and to perform other procedures that duplicate those of the engagement team.

Of course, issues should be raised by a reviewer if they are identified during the course of the procedures performed. However, by mandating separate determinations and judgments to be made by the reviewer, the focus of the Proposed Standard is the reviewer's own basis for the determinations he or she makes in the engagement quality review, rather than the reviewer's consideration of the judgments and conclusions reached by the engagement team in the audit. The judgments the reviewer makes will likely be seen as wholly separate from, rather than enhancing or confirming, those of the engagement team.

We believe firms, clients, and investors should continue to expect engagement partners to make reasonable judgments. Engagement quality reviews, along with the other quality control processes, combine to provide a firm with reasonable assurance about the effectiveness of its system of quality control, as is required. However, we see neither a purpose nor benefit in the redirection of focus of the engagement quality review or from the additional costs that will undoubtedly be incurred.

Our concerns are compounded by the new "know or should know" standard that changes the basis upon which the reviewer can concur in the issuance of the report. Under the current interim standard, the reviewer could concur so long as "no matters have come to his or her attention that would cause the [reviewer] to believe" that the financial statements did not conform to GAAP in all material respects or that the audit was not performed in accordance with GAAS. This is a "negative assurance" standard. The Proposed Standard, in effect, requires the reviewer, like the engagement partner, to determine that he or she has sufficient grounds to positively concur with the issuance of the report. It converts the engagement quality reviewer's conclusion to one that requires an



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affirmative finding or representation that, by definition, must be based on the performance of sufficient procedures to support the finding or representation.

We have a number of concerns about the proposed change in approach to an engagement quality review. First, the requirement that the reviewer make a positive determination about whether the report should be issued is directly contrary to the objective of the review; it comes far too close to, or could even be said to replicate, the judgment made by the engagement partner. Second, because of the limitations on what a reviewer can do without impairing objectivity, the reviewer's conclusion by extension will be based on limited information. The information gap between what the engagement partner knows and the engagement quality reviewer knows, will necessarily -- but we suggest inappropriately -- raise the question about what the reviewer *should have known*. Third, the introduction of a "should know" standard would be likely to have unintended consequences given the focus it brings to the potential for being second-guessed, particularly in the absence of an objective standard or specific direction about what is required to comply. It is reasonable to assume that many reviewers will interpret the required procedures in such a way that results in significant additional work for the purpose of anticipating a defense to any subsequent challenge.

We do not believe that imposing these kinds of requirements directly on the engagement quality reviewer will result in commensurate benefit to audit quality. We believe that a reviewer who conscientiously performs the procedures outlined in paragraph 8, as amended by our proposed revisions below, will appropriately contribute to audit quality by focusing on the significant matters addressed by the engagement team and providing an independent review of the engagement team's judgments and support for those judgments.

The following sections explain in more detail our concerns with the particular sections of the standard and set forth our recommended changes to the Board's proposal to address our concerns. We believe that our recommended changes are consistent with the objective we proposed.

Scope of Review

Paragraphs 7 and 8 prescribe general standards and specific procedures for conducting the engagement quality review. We generally agree with the nature of these procedures to be performed. However, we recommend a change to paragraph 7 and certain changes in the text of the paragraph 8 (set forth below) to clarify what procedures will satisfy the reviewer's responsibility to make the requisite evaluation and to avoid any suggestion that the reviewer is required -- or indeed able -- to duplicate the work of the engagement team or to make independent judgments about matters that are the responsibility of the engagement team.

These recommended changes included herein also would make the expected level of work more clear and avoid a fundamental change in the nature of the review function, which could otherwise potentially compromise the important principles of objectivity underlying the standard. The standard, we believe, should reinforce, not diffuse, the accountability of the engagement partner.



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Based on the foregoing, we recommend that the Board consider revising paragraphs 7 and 8 of the Proposed Standard. In addition to changes to implement our comments above, we believe certain provisions in paragraph 8 should be clarified to provide more certainty about how to satisfy the presumptively mandatory requirements in each of these sections:

7. The engagement quality reviewer should evaluate ~~include an evaluation of the significant judgments made by the engagement team and the significant conclusions reached by the engagement team in forming the overall conclusion on~~ in conducting the engagement and in preparing the engagement report, if a report is to be issued. ~~To identify and evaluate the significant judgments and conclusions, The evaluation should be conducted by~~ the engagement quality reviewer should include through discussions with the person with overall responsibility for the engagement, discussions with other members of the engagement team as ~~necessary~~ appropriate, and other procedures, as described in paragraphs 8 and 9.

8. As part of performing the engagement quality review, the engagement quality reviewer should:

- a. **Obtain an understanding of the ~~firm's recent engagement experience with the company and~~ risks identified in connection with the firm's client acceptance and retention process for the company.**
- b. **Obtain an understanding of the company's business, significant activities during the current year, and significant financial reporting issues and risks through discussions with the person with overall responsibility for the engagement, discussions with other members of the engagement team, as appropriate, and the performance of the procedures enumerated in the subparagraphs below.**
- c. **Review the engagement team's evaluation of the firm's independence in relation to the engagement (i.e., the communication with the audit committee required by Rule 3526, Communication with Audit Committees Concerning Independence, formerly Independence Standards Board Standard No. 1, Independence Discussions with Audit Committees).**
- d. **~~Evaluate~~ Review engagement planning, including (1) the judgments made about materiality and the effect of those judgments on the engagement strategy and (2) the identification of significant risks of material misstatement to the financial statements and the risks of material weakness in internal control over financial reporting, including fraud risks, and the plan for and performance of engagement procedures in response to those risks.**
- e. **~~Evaluate~~ Review judgments made about (1) the materiality and disposition of corrected and uncorrected identified misstatements and (2) the severity and disposition of identified control deficiencies.**



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- f. ~~Determine if appropriate consultations have taken place on difficult or contentious matters.~~ Review the documentation, including conclusions, of such consultations that have taken place on significant difficult or contentious matters.
- g. Read the financial statements, management's report on internal control over financial reporting, or other information that is the subject of the engagement and the engagement report (if an engagement report is to be issued) for the period covered by the engagement and for the prior comparative periods presented.
- h. Read other information in periodic filings and offering documents, as applicable, containing financial statements that are the subject of the engagement and are to be filed with the SEC and evaluate whether the engagement team has taken appropriate action with respect to material inconsistencies with the financial statements or material misstatements of fact of which the engagement quality reviewer is aware.
- i. ~~Determine if~~ Review whether appropriate matters of which the engagement quality reviewer is aware have been communicated, or identified for communication to the audit committee, management, and other parties, such as regulatory bodies.
- j. Review the engagement completion document and confirm with the person with overall responsibility for the engagement that there are no significant unresolved matters.

Note: Matters of which the engagement reviewer is “aware” are those matters that have come to the attention of the reviewer during the course of performing the procedures required by this standard.

Engagement Quality Reviewer Risk Assessment

Paragraph 9 of the Proposed Standard requires the reviewer to identify areas within the engagement that pose a “higher risk.” The term “higher risk” in that paragraph is not, however, directed to the potential for material misstatements or any other objective standard. Rather, the standard focuses on the “higher risk” that the engagement team failed to obtain sufficient competent evidence or reached an inappropriate conclusion. For the areas that pose such “higher risk,” the engagement quality reviewer is required to evaluate whether the engagement team performed procedures that were responsive to those risks, whether the judgments made by the engagement team were reasonable in the circumstances, and whether the results of the procedures support the engagement team’s overall conclusion.

We believe it is important that the engagement quality reviewer understand and review the significant risks of material misstatement to the financial statements and the risks of material



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weakness in internal control over financial statements identified by the engagement team and the engagement team's response to such risks. We do not believe that requiring a separate assessment of the risk that the engagement team failed to obtain sufficient competent evidence or reached an inappropriate conclusion is workable or consistent with the objective of an engagement quality review.

First, we question how the engagement quality reviewer would make such a determination. For example, what considerations would be deemed sufficient to support this determination, particularly without the benefit of information available in hindsight when his or her review is scrutinized? The standard does not articulate any procedures for making this determination, other than referring to the procedures in paragraphs 7 and 8 and "other relevant knowledge possessed by the engagement quality reviewer." Second, we note the Board's use of the term "higher risk." Being a relative term, it implies that there should always be some areas of higher risk, even though there might be no audit areas that pose a sufficiently high risk to justify further consideration or action. Third, we believe this requirement to be more concerned with having the reviewer make risk assessments separate from the engagement team, rather than reviewing the engagement team's own judgments for reasonableness. We question the focus of this requirement and the extent to which it will result in improvement to audit quality. Finally, we note that paragraph 12, both as proposed and consistent with our recommended revision, already contains a sufficient provision to prevent engagement quality reviewers from concurring with the issuance of the engagement report if, based upon the engagement quality review procedures performed, the reviewer believes that the engagement team failed to obtain sufficient competent evidence in accordance with PCAOB standards or reached an inappropriate conclusion about the subject matter of the engagement.

We recommend that the Board modify the proposed requirement in paragraph 9 to refocus it on whether important matters were identified during the engagement quality review that were not previously identified by the engagement team. Those matters should include the significant risks of material misstatement to the financial statements, significant risks of material weakness in internal control over financial reporting, and significant difficult or contentious matters where consultation by the engagement team should be considered that the engagement team might not have identified. If such matters are determined to exist, the engagement quality reviewer should be required to communicate these matters to the engagement team and assess whether the engagement team responds or has responded appropriately.

As such, we recommend that paragraph 9 be revised to read as follows:

9. Based on the procedures performed in accordance with paragraphs 7 and 8, and the engagement quality reviewer's knowledge, the engagement quality reviewer should assess whether any of the following matters were not previously addressed by the engagement team:

- **significant risks of material misstatement to the financial statements,**
- **significant risks of material weakness in internal control over financial reporting, or**
- **significant difficult or contentious matters where consultation should be considered by the engagement team.**



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If the engagement quality reviewer believes that there are such risks or matters, he or she should communicate that to the engagement team and then assess whether the engagement team has responded appropriately.

Review of Engagement Documentation

Paragraph 10 of the Proposed Standard would require the engagement quality reviewer to evaluate the engagement documentation. In particular, it requires the reviewer to evaluate whether the documentation “is appropriate in the circumstances and consistent” with the Board’s AS 3.

We believe audit documentation is important and we support the Board’s proposed requirement for an engagement quality reviewer to assess whether the engagement documentation supports the conclusions reached by the engagement team with respect to the matters reviewed by the engagement quality reviewer. However, we believe that the Proposed Standard, if not modified, could impose substantial additional burdens on the engagement quality reviewer to review the adequacy of documentation rather than the appropriateness of the significant accounting and auditing judgments made by the engagement team, and that result would not meaningfully enhance audit quality. We therefore recommend that the standard be modified in the following respects.

First, we believe the requirement to evaluate documentation should be limited to assessing that which is reviewed in connection with the procedures required by paragraphs 7 - 9 of the Proposed Standard. Absent such a limitation, the Proposed Standard might be interpreted to extend the engagement quality reviewer’s responsibilities to require him or her to conduct a separate review of all or much of the engagement documentation.

Second, we believe that the final standard should omit the requirement that the engagement quality reviewer evaluate whether the audit documentation is consistent with AS 3. We do not believe that this specific requirement is consistent with the overall objective of the engagement quality review, nor do we think it will meaningfully enhance audit quality. The engagement partner has primary responsibility for performance of the audit, including performing a review of the documentation for compliance with AS 3. It is not, and should not be, the engagement quality reviewer’s responsibility to duplicate that evaluation. Furthermore, we do not believe it is appropriate or necessary to single out any particular auditing standard for this type of compliance check by the reviewer.

We believe requirements in paragraphs 9 and 10 of the Proposed Standard potentially duplicate other requirements of AS 3. In addition, paragraph 13 of AS 3 requires that the engagement team “identify all significant findings or issues in an engagement completion document.” Paragraph 13 further states that “this document, along with any documents cross-referenced, should collectively be as specific as necessary in the circumstances for a reviewer to gain a thorough understanding of the significant findings or issues.” In our view, a qualified engagement quality reviewer should be able to achieve the objectives for the engagement quality review by performing the procedures outlined in paragraphs 7 and 8 of the Proposed Standard, as amended by our proposed revisions above, which reflect existing requirements and would include reviewing the engagement completion document.



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Third, we recommend that the Board revise paragraph 10 to make it clear that the scope of the engagement quality review is to assess whether the documentation that the reviewer selected for review supports the conclusions that were reached by the engagement team. That assessment will include considering significant risks of material misstatement to the financial statements and the risks of material weakness in internal control over financial statements and significant judgments by the audit team. Our recommended change, however, eliminates an implication that paragraph 10 creates a more general requirement to assess matters that are not encompassed by the procedures set forth in paragraphs 7 - 9.

Accordingly, we recommend that paragraph 10 of the Proposed Standard should be revised to read as follows:

10. Engagement Documentation. Based upon the procedures performed in accordance with paragraphs 7, 8, and 9, the reviewer should assess whether the engagement documentation reviewed during the course of the engagement quality review supports the significant conclusions reached by the engagement team.

Concurring Approval of Issuance

Paragraph 12 of the Proposed Standard provides that the engagement quality reviewer cannot provide “concurring approval” of the issuance of an engagement report if he or she “knows or should know” that any of four enumerated conditions exist.

We believe that the engagement quality reviewer’s concurrence is an important contribution to audit quality. We agree with the Board’s enumeration of the four conditions that, if present, would preclude the engagement quality reviewer from concurring with the issuance of the engagement report. We also support the requirement that the engagement quality reviewer consider the knowledge obtained in performing the review in accordance with the standard.

However, we believe that the inclusion of the legalistic “knows or should know” formulation for approval in auditing standards is neither necessary nor appropriate. This terminology would likely lead to misunderstanding and inconsistent application of the standard. For example, referring to what the reviewer “knows, or should know based upon the requirements of this standard” implies that the reviewer must perform sufficient procedures under the requirements of the standard to “know” that the four specified conditions do not exist. This would likely lead engagement quality reviewers to engage in substantial procedures to conclude that they do not know that any of the specified conditions are present. The term “should know” is even more troubling. It inherently creates a potential for post-hoc questioning of whether an engagement quality reviewer should have identified a condition that would have precluded him or her from concurring in the issuance of the engagement report. Accordingly, we believe that engagement quality reviewers will be overly focused on being second-guessed as to what they should have known, if a problem with the audit is later identified, rather than on assisting the engagement team by reviewing significant judgments and conclusions.



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As a result, the engagement quality reviewer would likely spend substantially more time, perform substantially more procedures and incur more costs than the reviewer would otherwise consider necessary, or we believe appropriate, in connection with a review. We strongly believe that the cost-effective improvement to audit quality should be the primary objective. We do not believe that inclusion of a “know or should know” standard of performance for the engagement quality reviewer furthers that objective. We recommend that paragraph 12 of the Proposed Standard be revised to remove the words “knows, or should know” by either conforming to the language used in ISA 220³, or alternatively, as follows:

12. The engagement quality reviewer must not ~~provide concurring approval of~~ concur with the issuance of an engagement report if, he or she knows, or should know based upon his or her review in accordance with the requirements of this standard, the reviewer believes that (1) the engagement team failed to obtain sufficient competent evidence in accordance with the standards of the PCAOB, (2) the engagement team reached an inappropriate overall conclusion on the subject matter of the engagement, (3) the firm's report, if a report is to be issued, is not appropriate in the circumstances, or (4) the firm is not independent of its client.

We believe that the proposed language retains the essence of the standard—that the reviewer cannot concur if he or she believes, based on the review, that any of the four enumerated conditions are present. However, it eliminates the inappropriate “knows or should know” standard.

Scope of Proposed Standard

While we acknowledge the Board’s desire for the engagement quality review standard to apply to all engagements performed in accordance with the standards of the PCAOB, the requirements in the Proposed Standard are so specifically tailored to financial statement audits and integrated audits that it would be difficult to apply some requirements to other types of engagements with any consistency among auditors. For some engagements, it may be appropriate to presume that certain requirements do not apply (for example, reading management’s report on internal control would not apply in a review of interim financial statements). However, in other situations, the Board’s intent is less clear. For example, it is unclear: a) to what extent, if any, obtaining an understanding of significant financial reporting issues and risks (paragraph 8(b)) would apply when reviewing an attestation engagement on the assessment of compliance with servicing criteria under the SEC’s Regulation AB; and b) which “prior period” is being referenced (paragraph 8(g)) with respect to a review of interim financial information.

Furthermore, with respect to the evidence required to be obtained (“sufficient competent evidence”), and the nature of the affirmative conclusion, the Proposed Standard appears to place the engagement quality reviewer in a position of having to obtain more evidence and to provide a

³ Paragraph 22(c) of Proposed and Redrafted ISA 220 requires the reviewer to document that “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.”



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higher level of assurance than the engagement team for certain engagements – for example, a review of interim financial information or a comfort letter for underwriters.

More specifically regarding a review of interim financial information, we are concerned that the requirements of the Proposed Standard are not consistent with the objective of a review of interim financial information. The objective of a review of interim financial information is “to provide the accountant with a basis for communicating whether he or she is aware of any material modifications that should be made to the interim financial information for it to conform with generally accepted accounting principles.”⁴ Toward that objective, a review consists principally of analytical procedures and inquiries of management. Some examples of what we believe to be inconsistencies between the requirements of the Proposed Standard and a review of interim financial information follow:

- Paragraphs 8d and 10 of the Proposed Standard include requirements for the engagement quality reviewer to evaluate the engagement team’s identification of, and responses to, significant risks. While a review of interim financial information involves assessment of risk in designing appropriate analytical and inquiry procedures, the terminology used in the Proposed Standard relates to an audit engagement, and we ordinarily would not expect an engagement team’s documentation in a review of interim financial information to include explicit risk assessments. Accordingly, the Board’s expectation of the engagement quality reviewer concerning risk assessment in a review of interim financial information is unclear.
- Paragraph 9 would require the engagement quality reviewer to assess whether there are areas within the engagement that pose a higher risk that the engagement team failed to obtain sufficient competent evidence or to reach an appropriate conclusion. As obtaining sufficient competent evidence is not a part of a review of interim financial information, we believe paragraph 9 will result in confusion and inconsistent practice in a review of interim financial information, notwithstanding the phrase “or to reach an appropriate conclusion.” Paragraph 12 also refers to sufficient competent evidence.
- Paragraph 12, as proposed, requires the engagement quality reviewer to provide an affirmative conclusion. Given that the objective of a review of interim financial information is to provide negative assurance, we do not believe it is appropriate for the engagement quality reviewer to reach a conclusion that is different than and goes beyond that which is required of the engagement team.

The Board therefore should identify the engagement quality review procedures required for interim reviews, provide clarity regarding the applicability of the procedures, and modify the conclusion to be reached by the engagement quality reviewer in connection with interim reviews. Specifically, the Board should include in the final standard an additional section, analogous to paragraph 7, that requires the engagement quality reviewer, in a review of interim financial information, to “discuss significant matters identified and addressed in connection with the review.” Similarly, the final standard should require that only a subset of procedures set forth in paragraph 8 (specifically those set forth in subparagraphs 8(g), 8(h), 8(i), and 8(j), as revised pursuant to the suggestions herein) be completed for interim reviews. Finally, the final standard should clarify that the engagement

⁴ AU 722.07



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quality reviewer is required to provide only negative assurance of concurring approval in the context of an interim review, consistent with the overall conclusion of such a review.⁵

We also recommend that the Board reconsider the practicality of applying the Proposed Standard to engagements other than financial statement audits, integrated audits, and reviews of interim financial information. If the Board believes engagement quality reviews are desirable for such engagements, we believe that the Board should develop a separate standard that allow the procedures to be tailored appropriately to the engagement circumstances. For example, we believe that a requirement to apply an auditing standard to an engagement performed in accordance with attestation standards would result in confusion and inconsistent practice. Accordingly, we believe any engagement quality review requirement for attestation engagements should be provided for in the attestation standards rather than the auditing standards.

Objectivity of the Engagement Quality Reviewer

Paragraphs 5 and 6 of the Proposed Standard address the objectivity of the engagement quality reviewer. At a minimum, we are concerned with the Proposed Standard's lack of clarity regarding objectivity.

The existing standard includes the concept of objectivity, but it focuses on the engagement quality reviewer's carrying out of his or her responsibilities with objectivity. Paragraph 5 of the Proposed Standard states that "the engagement quality reviewer must...maintain objectivity with respect to the engagement and the engagement team" (emphasis added). It is unclear whether the Board intends through this provision to limit somehow the engagement quality reviewer's interaction with the engagement team. For example, the proposed language could be interpreted such that the engagement quality reviewer would be precluded from working contemporaneously with a member of the engagement team (on a separate engagement, for example). Similarly, it is unclear whether the Board intends that objectivity be considered impaired if the engagement quality reviewer functions as the "performance manager" or mentor for a member of the engagement team, or recently supervised a member of the engagement team on an unrelated engagement. If interaction between the engagement quality reviewer and the engagement team were to be limited, we believe audit quality would be diminished. We also believe identifying engagement quality reviewers that have limited interaction, in general, with the members of the engagement team could be burdensome for registered firms, particularly smaller firms. We recommend that the Board's reference to objectivity with respect to the engagement team be eliminated, but in any event, the Board's intent should be clarified.

Furthermore, the note to paragraph 6 of the Proposed Standard and footnote 19 of the Release also could be interpreted to limit the discussions between the engagement team and the engagement quality reviewer. The note to paragraph 6 states the following: "The engagement team may consult with the engagement quality reviewer on matters during the course of the engagement. When participating in such consultations, the engagement quality reviewer should not participate in a manner that would compromise his or her objectivity with regard to the engagement" (emphasis

⁵ Our concerns regarding the proposed requirement for an affirmative conclusion by the engagement quality reviewer in an audit engagement are included in this letter under "Concurring Approval of Issuance."



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added). We believe that consultation is an important element of audit quality and that the standard should encourage consultation with the engagement quality reviewer.

To avoid the unintended consequence of limiting communications between the engagement team and the engagement quality reviewer that we do not believe compromise objectivity, we recommend:

- Replacing the language in paragraph 5 with language similar to that of QC Section 20, so that it states the following: “Engagement quality reviewers must be independent of the company and perform all professional responsibilities with integrity, and maintain objectivity in discharging professional responsibilities.”⁶
- Removing the second sentence of the note to paragraph 6. If the Board is concerned about the engagement quality review partner making an objective assessment, the standard could include language similar to that in the Board’s interim standard on concurring reviews as follows:

“When discussion occurs with the concurring partner reviewer on an accounting, auditing, or financial reporting matter during the engagement, the audit engagement partner ordinarily should develop an initial resolution to the matter before discussion with the concurring partner reviewer.”

We note this language appears on page 11 of the Board’s Release. Incorporating this language in the standard will make it clear that the Board is not intending to limit communications between the engagement quality reviewer and the engagement team or change the manner in which the two interact.

Finally, while we agree with the requirement in paragraph 6 of the Proposed Standard that the engagement quality reviewer should not make decisions on behalf of, or assume any responsibilities of, the engagement team, situations sometimes arise when a client may contact an engagement quality reviewer. We recommend that the standard include guidance that communications between the engagement quality reviewer and management or the audit committee would not necessarily compromise objectivity. In addition, we recommend that the standard include the guidance set forth below that is in footnote 3 of the Board’s interim standard on engagement quality reviews.

A client may contact the concurring partner reviewer with respect to matters requiring immediate attention when the audit engagement partner is not available because of illness, extended travel or other reasons. When a concurring partner reviewer is thus required to deal with an accounting, auditing or financial reporting matter, he or she should advise the audit engagement partner of the facts and circumstances so that the audit engagement partner can review the matter and take full responsibility for its resolution.

Documentation of an Engagement Quality Review

Paragraph 14 of the Proposed Standard, regarding documentation of an engagement quality review, sets forth a documentation standard that is separate and apart from, and incremental to, AS 3. We

⁶ See PCAOB Interim Standards, QC 20.09.



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believe some aspects of paragraph 14 are unclear and may lead to significant divergence in practice, and it is unclear to us why the existing requirements of AS 3 are not sufficient. AS 3 requires that audit documentation reflect, among other things, the nature, timing, extent, and results of the procedures performed, evidence obtained, and conclusions reached, and who reviewed the work and when. We recommend that the Board consider simply indicating that the requirements of AS 3 apply to an engagement quality review.

Alternatively, we recommend that the Board consider including a requirement consistent with paragraph 27 of the International Auditing and Assurance Standards Board's Proposed Redrafted ISA 220, *Quality Control for an Audit of Financial Statements*, which states:

The engagement quality control reviewer shall document, for the audit engagement reviewed, 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 date of the auditor's report; 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.⁷

If the Board decides to retain a new set of documentation requirements as proposed in paragraph 14 of the Proposed Standard, we are concerned particularly that the Board's intent in paragraphs 14(b) and (e) is unclear as described in the following paragraphs.

Paragraph 14(b) requires that the areas of the engagement subject to the engagement quality review be documented. In our view, an entire engagement is subject to the engagement quality review. However, if that interpretation is what the Board intended, it would not seem necessary to document that the engagement was subject to an engagement quality review, as that point would be self-evident from the engagement quality reviewer's concurring approval of issuance of the auditor's report. If the Board's intention is that the documentation reflect which individual work papers are reviewed or something else, we recommend that the Board clarify that point.

Paragraph 14(e) requires that the results of the review procedures be documented. We believe some auditors may view "the results of the review procedures" to be whether issuance of the auditor's report is approved. If this interpretation is correct, this requirement is redundant with paragraph 14(f) which requires documentation of whether the engagement quality reviewer provided concurring approval of issuance. We believe other auditors may view "the results of the review procedures" to denote a record of considerations made by the engagement quality reviewer, questions asked of the engagement team (e.g., review notes) with documentation of the engagement team's responses, etc. The latter meaning would result in an effort substantially incremental to practice under the Board's interim standard and the need for a significant increase in engagement

⁷ Our concerns regarding the proposed requirement for an affirmative conclusion by the engagement quality reviewer in an audit engagement are included in this letter under "Concurring Approval of Issuance."



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quality reviewer resources, with minimal benefit. We recommend that the Board eliminate paragraph 14(e) because it is redundant with paragraph 14(f).

Engagement Partner Movement to Engagement Quality Reviewer

Under the Board's interim standards, the engagement partner is precluded from serving as the engagement partner (for some period less than five years) and then moving directly into the role of concurring review partner for the remainder of the five-year period of service that is permitted. Specifically, the Board's interim standards state, ". . . a prior audit engagement partner should not serve as the concurring partner reviewer for at least two annual audits following his or her last year as the audit engagement partner." We believe that this requirement is appropriate and should be retained in the final standard.

Effective Date of the Proposed Standard

As proposed, the standard would be effective for reports issued on or after December 15, 2008. We are concerned that the proposed effective date would not permit sufficient time for registered public accounting firms to implement the new engagement quality review requirements. The effective date should provide all registered public accounting firms with sufficient time to (1) adopt policies and procedures consistent with the new standard, (2) train their personnel in the requirements of the new standard, and (3) assign qualified engagement quality reviewers consistent with their system of quality control.

We also believe that the effective date should be linked to the beginning of an engagement period. By linking the effective date to the beginning of the engagement period rather than the report issuance date, the new requirements would (1) be known and anticipated as of the beginning of the engagement period, (2) allow the assigned engagement quality reviewer to comply with the requirements throughout engagement planning and execution, and (3) be in place for each quarterly review conducted under AU section 722, *Interim Financial Information*.⁸ In this manner, adoption of the new standard would be more effective and efficient.

To the extent that the new standard contains more extensive requirements than the Board's interim standard, the PCAOB should delay the effective date to annual periods beginning no earlier than twelve months after SEC approval to provide adequate time for firms to prepare for adoption.

* * * * *

We reiterate our concern about what we perceive as a fundamental change in the nature and scope of an engagement quality review in the Proposed Standard and a divergence from international auditing standards, without a demonstrated accompanying benefit relative to the increase in cost. If the Board does not make significant modifications to the Proposed Standard before adoption of the final standard to address the matters raised in our comment letter, we recommend that the Board conduct a field test of the Proposed Standard prior to approval of a final standard. We envision that a field test would involve a sample of engagements for which the Board's standard, after deliberation of comment letters, would be applied. The Board, with the assistance of its standard-

⁸ Our concerns regarding the requirements of the proposed standard relative to reviews of interim financial information are included in this letter under "Scope of Proposed Standard."



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setting and inspection staffs, could monitor consistency of interpretation and application and identify any areas which result in confusion and/or unintended depth of review. In addition, inspectors could evaluate the quality of reviews, and the Board could evaluate increases in cost. The results of the field test could then be used to refine and/or support the provisions of a final standard. We would be willing to participate in such a field test.

In addition, absent significant modifications to the Proposed Standard, we have concern whether some required reviews can be performed in a timely manner prior to issuance of financial statements within the SEC's accelerated filing deadlines. Accordingly, absent significant modifications, we recommend that the PCAOB discuss with the SEC the impact of the standard on issuers' ability to meet filing deadlines, and whether such deadlines would need to be modified.

If you have questions about our comments or other information included in this letter, please do not hesitate to contact Craig Crawford, (212) 909-5536, ccrawford@kpmg.com or Glen Davison, (212) 909-5839, gdavison@kpmg.com.

Very truly yours,

KPMG LLP

cc: PCAOB Board Members:

Mr. Mark W. Olson, Chairman
 Mr. Daniel L Goetzler
 Mr. Willis D. Gradison, Jr.
 Mr. Charles D. Niemeier

SEC Commissioners:

Mr. Christopher Cox, Chairman
 Mr. Paul S. Atkins
 Ms. Kathleen L. Casey

Mr. Thomas Ray, Chief Auditor and Director of Professional Standards – PCAOB
 Mr. Conrad Hewitt, Chief Accountant, Office of the Chief Accountant – SEC
 Mr. John W. White, Director, Division of Corporation Finance – SEC
 Dr. Zoe-Vonna Palmrose, Deputy Chief Accountant for Professional Practice – SEC

May 9, 2008

Office of the Secretary
PCAOB
1666 K Street NW
Washington, D.C. 20006-2803

Re: PCAOB Rulemaking Docket Matter No. 025

We are pleased to have this opportunity to present the comments of Mayer Hoffman McCann P.C. (MHM) in response to the PCAOB proposed standard for engagement quality review. Though MHM in association with CBIZ is listed by Accounting Today as the eighth largest accounting services provider in the US, we are a relatively new entity representing an amalgamation of many smaller CPA firms. We have a growing SEC practice and are committed to maintaining the high level of service we give to our existing and future clients. We have created a culture revolving around a strong national office group which is actively involved in the designation of audit shareholders and concurring (engagement quality) reviewers for each of our SEC clients. Though we agree with many of the concepts discussed in the release, we are concerned that audit committees may use the requirements as another basis for engaging larger firms. It is based in part on that concern that we provide our comments. As you have requested, we will follow the format of your questions and intersperse our comments in what we believe is the appropriate response to the question.

Engagements for which an engagement quality reviewer is required

We believe the standard should include an overall objective of the engagement quality review and should focus on the skills that the reviewer must have in both business, but not necessarily the industry in which the client operates, and SEC filing matters. As a growing firm, we designate our quality reviewers as a preapproved group based primarily on their skill and experience in handling different audit assignments and background in handling SEC matters. Thus we would define the quality review person as an individual with general business acumen who provides an independent and final review of the work performed by the firm to judge whether the audit work papers support the issuance of an opinion in conformity with the PCAOB auditing standards and GAAP.

We support a quality review being performed for all PCAOB engagements.

Competence, Independence, Integrity, and Objectivity

As the proposed standards have been described, it will be difficult for many accounting firms to comply if they are attempting to grow their practice. The proposed standard indicates that the

reviewer should be able to serve as the engagement partner for a similar client in a specialized industry. We believe a reviewer should have a strong background in accounting and auditing that can be supplemented by available literature and consultation with experts in specialized industries. Where we do have a specialized industry, we try to match the best individuals in our firm to handle the account, regardless of location, and then select quality reviewers based upon the needs that we perceive are necessary to best serve the engagement.

We believe that not only should the engagement quality reviewer be permitted to consult with the engagement team, but that the reviewer should also be encouraged to participate, if possible, in the fraud risk discussions and review the engagement planning prior to the commencement of audit fieldwork. The process of engagement review should be a dynamic and ongoing process. So long as the reviewer's involvement deals with issues and questions, their independence and objectivity should not be impaired. Rather it permits for a more timely identification of issues and makes the audit process more efficient and effective. Because of a variety of circumstances, not necessarily related to the audit engagement, the quality reviewer may have to be changed prior to the completion of the engagement. Accordingly, though the review of planning and inclusion in the fraud risk discussion is a goal it should not be set as a requirement but rather a preference and where employed should be well documented. We believe this needs to be stressed in the final release.

The standard should also clarify what is meant by "supervising the engagement team". Is the definition intended to include, as it does under the independence standards, many shareholders in the "chain of command" or was it meant to supervise the engagement team in the field? If not clarified, this requirement again will put a strain on the resources of firms that are building their practice. We for example are separated into three geographic regions and have designated three of our most experienced shareholders as Regional Attest Practice Leaders and have another shareholder, who is a member of the PCAOB's Standing Advisory Group, designated as our National Director of Professional Standards. We believe in our structure that all of these people are independent and objective and have assigned them to be the quality reviewers on a number of PCAOB audits. Accordingly we expect that the definition of "supervise the audit team" was not intended to be so broad as to preclude these types of individuals from performing engagement quality reviews. We ask that the final standard clarify this issue.

Scope of the review

The suggested scope and approach should provide a reasonable basis for the performance of the quality review. Since one of the objectives is to provide for the identification of "...significant problems in a timely manner for correction, without imposing unnecessary costs," we reiterate our belief that the involvement of the quality reviewer, as issues are raised, would be more audit efficient and effective than to wait for the reviewer to first gain knowledge of issues during their subsequent review.

Review of engagement documentation

The proposed standard will clarify and improve the requirements for the review of engagement documentation.

Timing of the review

As we have stated previously, we believe the review should be performed in stages. This will be especially important in multinational engagements where there may be several reviewers, who would be working at the request of an overall reviewer, looking at different aspects of an audit.

Concurring approval of issuance

The standard appears appropriate, except that we question how the staff intends to interpret the guidance that the quality reviewer needs to ascertain that the firm is independent. A quality reviewer would make an inquiry of the audit partner and generally have to rely on that answer. Presently there is nothing in the standard that indicates where the reviewer may gain knowledge of possible independence violations. However, if the reviewer were asked their view on a particular service offering and its impact on independence, we would expect that an inquiry would be made as to the ultimate resolution.

Documentation of an engagement quality review

We believe the standards are appropriate as stated.

If you have any questions regarding our comments, please contact Aram Kostoglian, Eastern Regional Attest Practice Leader at 212-244-1100, ext. 210 or Ernie Baugh, National Director of Professional Standards at 423-870-0511.

Very truly yours,

MAYER HOFFMAN McCANN P.C.



Paris La Défense, May 12, 2008

PCAOB

Mr. Gregory Scates, Deputy Chief Auditor

Mrs. Keesha Campbell, Assistant Chief Auditor

1666 K Street, NW

Washington, D.C. 20006

Re: Rulemaking Docket Matter No. 025 - Request for Public Consideration and Comment on Proposed Auditing Standard - Engagement Quality Review ("EQR") and Conforming Amendment to the Board's Interim Quality Control Standards

Madame, Sirs,

Mazars is an international organization of European origin, specialized in audit, accounting, tax and advisory services. Its integrated partnership assembles more than 8,000 professionals operating in 46 countries. Moreover, via the International Praxity Alliance of which Mazars is a founding member, the group can access the skills and expertise of a further 15,000 professionals in another 23 countries, all of whom possess a common desire to adhere to strong quality guidelines and a collective determination to exceed technical and ethical standards.

Mazars thus asserts itself as a strong challenger to the international market; thanks to its multicultural structure and complete range of services, the group is able to offer flexible, tailored solutions to large multinational firms and to those SMEs it assists in their development, as well as to high net worth individuals.

As of the 31st of August 2007, its turnover was 657 million euros. However, as of the 1st of January 2008, its pro forma turnover, taking into account those entities which have joined the group since the 1st September 2007, was approximately 675 million euros.

We are pleased to submit this letter in response to the request for the request for public consideration and comment from the PCAOB on its Proposed Auditing Standard – Engagement Quality Review and Conforming Amendment to the Board's Interim Quality Control Standards.

We will proceed with our comments in two ways:

- (1) General Comments on the Proposed Auditing Standard, and
- (2) Specific Comments with Responses to the PCAOB's 11 Questions.



2

1 General Comments on the Proposed Auditing Standard

Mazars agrees with the PCAOB that the timing is right to focus on another pillar of the audit quality: the engagement quality review. The International Federation of Accountants (IFAC) already focused on this issue in its standards ISQC1 and ISA 220, so convergence could certainly be found on the objective and principles of the engagement quality review, in order to achieve efficiency of the roll-out of the standard in a global organization.

Mazars also generally agrees with the proposed PCAOB EQR standard as follows:

- there should be only one EQR standard for audit engagements performed under the standards of the PCAOB,
- the EQR reviewer should not only be competent but should meet attributes of independence, integrity, and objectivity,
- the EQR should be considered as a process relying on a risk-based approach and requiring the engagement reviewer to focus on the significant judgments made by the engagement team,
- the review of the engagement documentation borrows requirements of AS3, Audit Documentation, (so that there is no need to re-invent the wheels with regards to new documentation requirements).

2 Specific Comments with Responses to the PCAOB's 11 Questions

2.1 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?

In general, Mazars agrees with all three aspects of Section A (page 7-8) regarding engagements for which an EQR is required: (1) The proposed EQR standard should be required for all engagements performed in accordance with the standards of the PCAOB (2) There are potential benefits to be gained from performing an EQR in order to comply with various attestation engagements (audits of financial statements, audits of internal control over financial reporting, and reviews of interim financial statements), and (3) This proposed EQR standard should be applicable to all registered accounting firms, newly registered and AICPA SECPS registered as of 2003.

Mazars suggested that the proposed auditing standard explicitly state an overall objective of an EQR or at a minimum establish specific requirements and provides clear directions applicable for EQR engagements. Establishing an overall objective of an EQR will serve as a roadmap enabling audit practitioners to apply the proposed EQR requirements in an efficient and effective manner. The vast majority of accounting and auditing standard-setters are hearing the complaints coming from the business and investment communities, academia, and public-at-large about the difficulties of understanding and applying certain new accounting and auditing standards. For instance, the PCAOB AS5, which was approved by the SEC on July 25, 2007 and which superseded AS2, had as one of its major overall objectives to get the auditors to assess risks and to focus on the greatest risks.



We believe that the overall objective of an EQR engagement should be to evaluate the significant judgments made by the engagement team and the conclusions reached in forming the overall conclusion on the engagement.

2.2 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 required?

Mazars believes that the proposed EQR which would supersede the PCAOB's interim concurring partner review requirement and would amend its interim quality control standards is an integral part of the overall quality control of a registered accounting firm and as such it should be required for all engagements performed in accordance with the standards of the PCAOB (audits of financial statements, audits of internal control over financial reporting, and reviews of interim financial statements).

Often referred reporting engagements will involve the component auditor confirming that their work has been conducted in accordance with PCAOB standards. To maintain this level of reporting, the introduction of the proposed standard would prompt the introduction of EQRs for component audits. However, in such circumstances second-sight judgments are best provided by instructing offices rather than through the involvement of a new partner at the component level by the reporting office. We recommend that the proposed standard should not apply by non-material component audits.

Given the extensive use of the ISA standards worldwide and the trend towards harmonization of accounting standards (US GAAP and IFRS), the PCAOB should consider adapting or harmonizing its proposed EQR standard to/with the international auditing standards so as to permit its use even by non-registered accounting firms (as a best audit practice).

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

The PCAOB interim quality control standards¹ on concurring partner review states that the concurring partner reviewer should have sufficient technical expertise and experience to perform an objective review of significant auditing, accounting, and financial reporting matters that come to his/her attention. The sufficiency of the technical expertise and experience depends upon circumstances of the engagement, including engagement personnel. The reviewer is also supposed to be knowledgeable about relevant specialized industry practices as well as SEC rules and regulations.

The proposed EQR puts emphasis on the notion of competence and adds on the notions of independence, integrity, and objectivity. The proposed EQR also establishes the reviewer's level of expertise and experience required to perform an objective EQR as the same as those of the person who has overall responsibility for the same type of engagement.

¹ Refer to Appendix E – Concurring Partner Review Requirement (Revised with an Effective Date of March 31, 2002)



Mazars agrees that the competence of an engagement reviewer as currently proposed is adequate. The partner-in-charge of the audit and the EQR engagement reviewer shall have the same equivalent level of qualifications and competency. However, Mazars believes that there is a distinction between qualification and competence which goes further than qualification. As such, Mazars supports the focus on the notion of competence. The notion of authority of the reviewer (standing or status) should also be considered given the role of the reviewer will require a certain level of authority, or veto right if you will, in order to ensure that their role is adequately viewed in the hierarchy of the respective firm. We believe this is important considering the interim standard requires a “concurring partner review” and this proposed standard would require a competent “engagement quality reviewer”, which may not necessary be a partner.

2 4 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?

Mazars agrees that the proposed EQR should allow the engagement team to consult with the engagement quality reviewer during the engagement provided that the engagement reviewer maintains his/her independence, integrity, and objectivity. Such consultation would not impair his/her objectivity assuming that he/she maintains his/her professional care and professional skepticism. Such interim consulting should be encouraged because it could serve to resolve audit engagement issues prior to issuance. The EQR reviewer could provide his/her input during the engagement while maintaining his/her independence (mental attitude and audit approach).

2 5 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?

Mazars believes that the descriptions of the scope and extent of engagement quality review procedures contained in pages 12 and 13 of this proposed EQR are appropriate. Further, Mazars notices that the requirements to evaluate significant judgments made by the engagement team and the conclusions reached in forming the overall conclusion on the engagement as well as the review procedures used to evaluate the engagement itself are similar to the requirements of the related standards of the IAASB (ISQC1 and ISA 220). As such, there are similarities between this proposed EQR standard and the standards of the IAASB with regards to scope and review procedures for engagement quality review.

2 6 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?

Paragraph C (page 12) of this proposed EQR standard states that “*the engagement quality review described in the proposed standard is a risk-based approach that would require the reviewer to focus on the significant judgments made by the engagement team, as well as the conclusions that*



the engagement team reached in forming its overall conclusion on the engagement and preparing the engagement report.”

Since the adoption of AS5 in July 2007, it is now a standard practice to use a risk-based approach when performing audit or review procedures. The risk-based approach, whether used to focus on the greatest risks or on the most significant judgments, is an approach that permits to identify significant engagement issues or audit risks.

Mazars believes that the risk-based approach to the EQR is sufficiently described by the proposed EQR.

2 7 Question 7: Are the proposed requirements for the review of the engagement team's documentation appropriate? If not, how should they be changed?

Mazars agrees that the proposed requirements for the review of the engagement team's documentation as described on page 14 are appropriate given the fact that it is limited to the areas reviewed (including the overall risk approach).

2 8 Question 8: Is the description of the timing of the engagement quality review, as proposed, appropriate? If not, how should it be changed?

Mazars believes that the description of the timing of the engagement quality review as per page 15 is appropriate as described. The proposed EQR standard requires the engagement quality reviewer to complete his/her work prior to providing concurring approval of issuance. However, the proposed EQR does not prescribe the timing of the review. This gives flexibility to an EQR reviewer to schedule his/her engagement review based on the size and complexity of the engagements and other circumstances as he/she sees fit. It almost introduces an element of professional judgment in selecting the timing of the EQR.

2 9 Question 9: Is the standard for the engagement quality reviewer's concurring approval of issuance appropriate? If not, how should it be changed?

Mazars believes that the standard for the engagement quality reviewer's approval of issuance is appropriate as described in Section D, page 15 and 16 of this proposed EQR standard. By making the release of the engagement report contingent upon the completion of the EQR engagement, this legitimizes the importance of the EQR. However, the proposed EQR standard is missing a formal process to resolve legitimate differences of opinion that could occur between the audit engagement team and the engagement quality reviewer. To simply state that the differences of opinion should be satisfactorily resolved first before any concurring review is approved is not adequate. Consequently, Mazars proposes that the PCAOB put some teeth to this process by requiring that any unresolved differences of opinion between the engagement team and the engagement quality reviewer be brought before the audit firm partners-in-charge of quality control or experts. At the minimum, the proposed standard should state that the resolution of any differences of opinion that could occur between the audit engagement team and the engagement



6

quality reviewer is a matter of a firm's policy, in other words should be resolved based on a firm's policies and procedures before issuance.

2 10 Question 10: Are the documentation requirements for an engagement quality review appropriate? If not, how should they be changed?

As described in Section E, page 17 and 18 of this proposed EQR standard, it appears that the documentation requirements for an EQR engagement are appropriate. This engagement documentation avoids the check-the-box approach and borrows heavily from AS3 requirements. However, Mazars would like to propose that the audit engagement document explicitly includes the rationale for selecting EQR reviewer as well as his/her compliance with requirements regarding competence, independence, integrity, and objectivity.

2 11 Question 11: 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?

Based on the review of the proposed EQR standard and our knowledge of AS3, it is Mazars' opinion that the proposed EQR standard should comply with provisions contained in AS3 as a whole rather than on a piecemeal basis so as to make both standards complementary and more effective.

We hope the above comments will be helpful and remain available for further observations. If you would like to discuss our submission further, please do not hesitate to contact us.

Yours sincerely,

A handwritten signature in blue ink, appearing to read 'J. Barlet'.

Jean-Luc Barlet
Risk Management & Audit Quality

McGladrey & Pullen

Certified Public Accountants

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May 12, 2008

Office of the Secretary
Public Company Accounting Oversight Board
1666 K Street, N.W.
Washington, D.C. 20006-2803

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

McGladrey & Pullen, LLP is pleased to submit written comments on the proposed auditing standard, *Engagement Quality Review and Conforming Amendment to the Board's Interim Quality Control Standards*. McGladrey & Pullen, LLP is a registered public accounting firm serving middle-market issuers.

McGladrey & Pullen, LLP supports the issuance of an engagement quality review standard that more clearly articulates the standards for performing an engagement quality review. However, we do have some concerns with specific aspects of the proposed standard as set forth in our responses to the questions posed in Release 2008-002 and in our other comments which follow.

Engagements for Which an Engagement Quality Review Is Required

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?*

We believe the standard should state an overall objective of the engagement quality review. We suggest the following overall objective:

"The objective of an engagement quality review is to provide an objective evaluation of the significant judgments made by the engagement team in (a) assessing the significant risks of material misstatement, (b) identifying and performing procedures that were responsive to those risks, (c) evaluating the adequacy of the audit documentation with respect to such risks, and (d) concluding on whether the results of the procedures support the engagement team's overall conclusions; and, to provide concurring approval of the engagement report prior to its issuance."

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 required?*

We believe that an engagement quality review should be required for all engagements performed in accordance with the *auditing standards* of the PCAOB. We are concerned, however, that because the proposed standard is written in the context of an audit of the financial statements or an audit of internal control over financial reporting that is integrated with an audit of the financial statements, it is not readily adaptable to certain engagements, such as those performed in accordance with AU 622, 634 and 722.

Qualifications of the Engagement Quality Reviewer

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

We believe that the qualifications of an engagement quality reviewer are appropriately described in the proposed standard. We note that the proposing release appropriately indicates that the engagement quality reviewer may seek assistance from others to supplement his or her own expertise and experience or where needed to complete the review in a timely basis. We suggest that similar language be included in the standard itself.

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?*

We believe the engagement team should be allowed to consult with the engagement quality reviewer during the engagement and that such consultation would not impair the reviewer's objectivity provided the engagement team first analyzed and appropriately documented the relevant facts, circumstances and professional standards, and the engagement team's conclusions with respect to the subject matter of the consultation.

The Engagement Quality Review Process

Scope of Review

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?*

We believe the scope and extent of the procedures set forth in paragraphs 7-10 of the proposed standard are generally appropriate. However, see our recommendations for modification of paragraphs 7-10 of the proposed standard set forth below, which we believe would appropriately distinguish the engagement quality reviewer's responsibilities from those of the engagement team.

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 the use of a risk based approach to the performance of the engagement quality review, however, we believe the focus of the risk assessment should be on the significant risks of material misstatement rather than on the risk that the engagement team failed to obtain sufficient competent evidence or reached an inappropriate conclusion because there is no generally accepted risk model against which to evaluate that risk. See our recommendations for modification of paragraphs 7-10 of the proposed standard set forth below.

Review of Engagement Documentation

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

We believe the engagement quality reviewer should have the responsibility to assess the adequacy of the audit documentation with respect to the areas reviewed, but we have recommended modifications to paragraph 10 of the proposed standard, as set forth below.

Timing of the Review

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

We believe the requirements for the timing of the engagement quality review, as set forth in paragraph 11 of the proposed standard, are appropriate.

Concurring Approval of Issuance

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

We believe the "know or should have known" standard, as set forth in paragraph 12 of the proposed standard is very problematic and that a better approach would be to establish a requirement that would preclude concurrence with issuance if the engagement quality reviewer "has not performed" the review in accordance with the requirements of the standard or, based on his or her review, the reviewer "knows" that the engagement team has failed to obtain sufficient competent evidence to support the engagement report or that the engagement report proposed to be issued by the firm is inappropriate. See our recommendations for modification of paragraph 12 of the proposed standard set forth below.

Documentation of an Engagement Quality Review

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

The documentation standards set forth in paragraph 14 of the proposed standard are generally appropriate; however, see our recommended modifications to those requirements set forth below.

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 believe there are no provisions of AS No. 3 not set forth in paragraph 14 of the proposed standard that would be applicable to the documentation of the engagement quality review.

Recommendations for Modifications to Specific Paragraphs of the Proposed Standard

Paragraph 7

7. The engagement quality review should include an evaluation of the significant judgments made by the engagement team and the significant conclusions reached ~~by the engagement team~~ in forming the overall conclusion on in conducting the engagement and in preparing the engagement report, if a report is to be issued. To identify and evaluate the significant judgments and conclusions, the engagement quality review should include discussions with the person with overall responsibility for the engagement, discussions with other members of the engagement team as deemed necessary by the reviewer, and other procedures, as described in paragraphs 8 and 9.

Paragraph 8

8. As part of performing the engagement quality review, the engagement quality reviewer should:

- a. **Read the engagement acceptance or continuance documentation and make inquiries of the engagement team to Obtain an understanding of the firm's recent engagement experience with the company and risks identified in connection with the firm's client acceptance and retention process.**
- b. **Read the engagement planning documentation, make inquiries of the engagement team and perform other procedures as deemed necessary by the reviewer to Obtain an understanding of the company's business, significant activities during the current year, and significant financial reporting issues and risks of material misstatement.**
- c. **Review the engagement team's documentation of its evaluation of the firm's independence in relation to the engagement.**

- d. Evaluate engagement planning, including (1) the judgments made about materiality and the effect of those judgments on the engagement strategy and (2) the identification of significant risks of material misstatement, including fraud risks, and (3) the plan for ~~and~~ performance of engagement procedures in response to those risks.
- e. Evaluate judgments made about (1) the materiality and disposition of corrected and uncorrected identified misstatements and (2) the severity and disposition of identified control deficiencies.
- f. Read the documentation of consultations that have taken place on difficult or contentious matters. ~~Determine if Evaluate whether~~ appropriate consultations have taken place on difficult or contentious matters that were subject to the engagement quality review procedures. ~~Review the documentation, including conclusions, of such consultations.~~
- g. Read the financial statements, management's report on internal control over financial reporting, or other information that is the subject of the engagement and the engagement report (if an engagement report is to be issued) for the period covered by the engagement and for the prior comparative periods presented.
- h. Read other information in documents containing financial statements that are the subject of the engagement to be filed with the SEC and evaluate whether the engagement team has taken appropriate action with respect to material inconsistencies with the financial statements or material misstatements of fact of which the engagement quality reviewer is aware.
- i. ~~Determine if Evaluate whether~~ appropriate matters that were subject to the engagement quality review procedures have been communicated, or identified for communication to the audit committee, management, and other parties, such as regulatory bodies.
- j. ~~Review~~Read the engagement completion document and confirm with the person with overall responsibility for the engagement that there are no significant unresolved matters.

Paragraph 9

9. Based on the procedures performed in accordance with paragraphs 7 and 8, and other relevant knowledge possessed by the engagement quality reviewer, the engagement quality reviewer should assess whether there are significant risks of material misstatement ~~areas within the engagement that were not identified by the engagement team~~ ~~pose a higher risk that the engagement team has failed to obtain sufficient competent evidence or reached an inappropriate conclusion.~~ For the ~~areas that pose any such risks,~~ the engagement quality reviewer should evaluate whether the engagement team performed procedures that were responsive to the ~~assessed risks,~~ the judgments made by the engagement team were reasonable in the circumstances and the results of the procedures support the engagement team's overall conclusion.

Paragraph 10

10. Evaluate *Engagement Documentation*. The reviewer should evaluate whether the engagement documentation of the matters that were subject to the engagement quality review procedures –

- a. ~~Is appropriate in the circumstances and consistent with the requirements of PCAOB Auditing Standard No. 3, *Audit Documentation* (AS No. 3),~~
- b. Indicates that the engagement team responded appropriately to matters that present a significant risk of material misstatement, and
- c. Supports the conclusions reached by the engagement team ~~with respect to the matters reviewed~~ and the conclusions and representations in the engagement report with respect to the matters reviewed.

Paragraph 12

12. The engagement quality reviewer must not provide concurring approval of issuance if he or she has not completed the engagement quality review in accordance with the requirements of this standard, or knows, or should know based upon the requirements of this standard, that (1) the engagement team failed to obtain sufficient competent evidence in accordance with the standards of the PCAOB, (2) the engagement team reached an inappropriate overall conclusion on the subject matter of the engagement, (3) the firm's report, if a report is to be issued, is not appropriate in the circumstances, or (4) the firm is not independent of its client.

Paragraph 14

14. Documentation of an engagement quality review should be included in the engagement documentation and should include information concerning:

- a. Who performed the engagement quality review,
- b. The areas of the engagement subject to the engagement quality review,
- c. Evidence that the procedures required by paragraphs 7-10 of this standard were performed by the engagement quality reviewer,
- d. When the review procedures were ~~performed~~completed,
- e. ~~The results of the review procedures~~Whether the engagement quality reviewer concurs with significant judgments made by the engagement team in the areas subject to the engagement quality review procedures, and
- f. Whether the engagement quality reviewer provided concurring approval of issuance.

Other Comments

Effective Date

As proposed, the standard would be effective for engagement reports issued (or the communication of an engagement conclusion, if no report is to be issued) on or after December 15, 2008. We are concerned that the proposed effective date would not permit sufficient time for registered public accounting firms to implement the new engagement quality review requirements. We also believe that the effective date should be linked to the beginning of an engagement period. By linking the effective date to the beginning of the engagement period rather than the report issuance date, the new requirements would (1) be known and anticipated as of the beginning of the engagement period, (2) allow the assigned engagement quality reviewer to comply with the requirements throughout engagement planning and execution, and (3) be in place for each quarterly review conducted under AU section 722, *Interim Financial Information*. In this manner, adoption of the new standard would be more effective and efficient.

The effective date should provide all registered public accounting firms with sufficient time to (1) adopt policies and procedures consistent with the new standard, (2) train their personnel in the requirements of the new standard, and (3) assign qualified engagement quality reviewers consistent with their system of quality control. Accordingly, we recommend that the PCAOB should delay the effective date to annual periods beginning no earlier than twelve months after SEC approval of the final standard.

Closing

Thank you for the opportunity to comment on this proposed standard. Questions concerning our comments should be directed to Bruce Webb, Executive Partner – National Office of Audit and Accounting (515.281.9240) or Scott Pohlman, SEC Coordinator (952.921.7734).

Very truly yours,

McGladrey & Pullen, LLP



1 MetLife Plaza,
27-01 Queens Plaza North
Long Island City, NY 11101

Joseph J. Prochaska, Jr
Executive Vice President
Finance Operations and Chief
Accounting Officer

Attention: Office of the Secretary
Public Company Accounting Oversight Board
1666 K Street, N.W.
Washington, D.C. 2006-2803

Re: PCAOB Rulemaking Docket 025

To whom it may concern:

MetLife, Inc. ("MetLife") appreciates the opportunity to comment on the Public Company Accounting Oversight Board's (the "Board") Proposed Auditing Standard, *Engagement Quality Review*. We support the Board's objective of enhancing the quality of financial statement audits as the quality of such audits is a critical element in establishing a basis for investor reliance.

In general, we strongly support any change to the Board's standards which would improve the quality and reliability of our audit reports. We are a strong advocate of the use of a principles-based approach. However, it appears to us that the proposed guidance seems to be more rules-based and provides extensive detail and structure that limits an accounting firm's ability to adapt the requirements of this guidance to the specific needs of an audit engagement. MetLife believes that there should be sufficient guidance for the principles to be understandable, operational and capable of being applied consistently in similar situations. The implementation of this rules-based guidance may require independent auditors to significantly change their current process and that would result in increased administrative costs, which will eventually be borne by the company and our shareholders, while potentially adding minimal value to the underlying quality of the audit. We think this would be contrary to the Board's stated intent to complete work "without imposing unnecessary costs."

We believe this proposed approach is a significant departure from the requirement currently in place, which allows the concurring partner to issue a conclusion if "no matters have come to his or her attention" that would cause the partner to believe that the audit was not in accordance with PCAOB standards or in conformity with

GAAP. This new proposal prohibits the concurring partner from providing approval if he or she “knows or should know” of an issue or a conclusion that was not in accordance with PCAOB standards or in conformity with GAAP. This changes the basis of concurring opinion from “negative assurance” to “positive assurance,” and while the Board acknowledges that a concurring review “should not perform procedures amounting to a re-audit,” including the phrase “should know” implies a duty to review a vast amount of audit evidence at his/her disposal. The breadth of evidence at the concurring teams’ disposal includes all documentation of the engagement and could effectively lead to an unnecessary re-audit at a significant additional cost to our shareholders.

Finally, the timing for completion of concurring reviews may negatively impact the quality of the audit. The standard would not change the requirement that auditors complete all procedures before issuing the concurring approval. This proposal creates a situation where the volume of documentation and audit work may increase significantly, yet the time to complete the concurring review is limited by the filing deadlines of the Securities and Exchange Commission. To address timing pressures, the proposed standard suggests that the reviewer may consult “at the time issues arise rather than at the conclusion of the engagement...” however, it also suggests that a resolution must be developed by the audit team prior to consultation. This has the potential to slow work on the audit, as issues are discussed and resolved on a case-by-case basis. In addition, the consultation process must be carefully conducted, so as to maintain the reviewer’s objectivity. The end result of the timing pressures created by the proposed standard, we believe, will be that a company must complete its financial statements and disclosures earlier, or that the accounting firm must increase its audit staff to meet the demands of this proposal. Both of these solutions will increase the cost to the audited company.

We are pleased to have this opportunity to share our thoughts and experiences.

If you have any questions regarding the information in this letter, please feel free to contact me at (212) 578-8846.

Sincerely,

A handwritten signature in black ink, appearing to be 'J. P. ...', written in a cursive style.

May 12, 2008

PIERCY BOWLER TAYLOR & KERN

Certified Public Accountants • Business Advisors

April 28, 2008

To: Office of the Secretary, Public Company Accounting Oversight Board

Re: PCAOB Rulemaking Docket Matter No. 025 — Engagement Quality Review

We are pleased to respond in this letter to the cited proposal contained in PCAOB Release 2008-002 (the Release).

We understand that the stated objective of Section 103 of the Sarbanes-Oxley Act (the Act) of 2002 is for the PCAOB to include a requirement for a concurring review in its auditing standards applicable to audits of issuers (as defined in the Act), and we share the Board's apparent view of the importance of the contribution to audit quality that such a standard can and should make.

We also understand the Board's concerns about the consistency of application of such a standard from firm to firm and from engagement to engagement and the ability of its inspectors to evaluate the scope of a given review in relation to such a standard. We believe our comments address these concerns consistently with the implied primary objective of the standard, which we take to be providing reasonable assurance of uniformly high quality engagement quality reviews in terms of their scope and execution.

In addition to responding below to the questions posed by the Board in the Release, we point out that the proposed standard (Appendix 1 to the Release), itself, is quite brief. We believe there is useful guidance in the Release but outside the proposed standard and that the final standard would be improved if some of that guidance were to be incorporated therein. For example, part B3 on p. 12 of the Release provides guidance as to how a contracted outside reviewer might become an "associated person of a registered public accounting firm."

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?*

We believe a stated objective for "engagement quality reviews" (as they are now proposed to be and hereinafter are called) would be an essential element in meeting the implied primary objective of the standard itself, as stated above.

Despite any stated objective of an engagement quality review, we believe that at the point of stating the objective, there should be a direct and proximate reference to the statement that appears in paragraph 6 of the proposed standard that the engagement quality reviewer does not relieve the primary engagement partner or equivalent from the final responsibility for issuing the firm's report(s).

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 required?*

We believe the final standard should clearly state that an engagement quality review is required only for (a) audits of the financial statements of issuers (as defined), (b) other attest services resulting in opinions intended for filing with the SEC or public distribution, (c) audits of the financial statements

(or financial statement information) of nonissuers that have a material effect on the financial statements of issuers, such as significant subsidiaries (including consolidated variable interest entities) and unconsolidated investees that are carried on the equity method of accounting, and (d) to enable approval of the issuance or updating under PCAOB Interim Auditing Standard AU sec. 711 (or a successor standard) of a consent intended for inclusion of an audit report in a federal securities filing. Significance of subsidiaries and unconsolidated investees that are carried on the equity method of accounting should be determined in such regard objectively by a definition containing criteria similar to those in Rule 1001(p)(ii) applicable to the phrase "play a substantial role in the preparation or furnishing of an audit report."

We believe the final standard also should state that engagement quality review procedures are not required to support or approve the issuance of a comfort letter to underwriters or others under PCAOB Interim Auditing Standard AU sec. 634 (or a successor standard) unless required by the underwriter or other intended recipient or by the issuing firm's quality control policies.

We also do not believe it is apparent by the language in Section 103 of the Act that Congress intended auditor services to undergo engagement quality reviews if the services do not involve issuance of an audit or attestation opinion, or a consent to include a report containing such an opinion in a federal securities filing. We further believe that (a) the level of assurance indicated or implied that results from a review of interim financial information conducted under PCAOB Interim Auditing Standard AU sec. 722 (or a successor standard) warrants the imposition of a mandatory engagement quality review and that (b) the additional constraints for timely reporting applicable to interim financial information would make it impractical to add another level of review. Therefore, for reviews of interim financial information, we are in favor of retaining only the burden of timely consultation with the assigned quality reviewer about matters identified in the review that involve a significant risk of material misstatement that is now set forth in SECPS §1000.39, Appendix E, item d.

We believe that an engagement quality review for audits of financial statements of other nonissuers conducted in conformity with PCAOB standards should be optional because we believe such a distinction as to the applicability of this requirement would be consistent with the intent of Congress as expressed in Sec. 103 of the Act and with the associated risks and needs of different classes of users.

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

We do not think so. The predecessor version of the proposed standard that is contained in SECPS §1000.39, Appendix E, that is incorporated by reference into §1000.08(f) and the PCAOB's Interim Quality Control Standards sec. QC 20.18, clearly required (and in our opinion, without justification) a concurring reviewer to be an equity owner (partner or shareholder) of the firm. To its credit, paragraph 2 of the proposed standard, however, states (although too subtly, in our view) that the engagement quality reviewer need not be an equity owner. Rather, paragraphs 3, 4 and 6 emphasize correctly that the critical attributes of the engagement quality reviewer are (a) competence and (b) independence, integrity and objectivity. However, Rule 2-01(f)(7)(ii)(B) of Reg. S-X similarly does not require equity ownership but does require that both engagement "partners" and concurring reviewers have "equivalent authority" to that of an equity partner. We believe the final version of the new standard should also require that an engagement quality reviewer possess the equivalent professional authority (but not the financial interest) of an equity owner to assure his or her independence, objectivity and the level of respect from the engagement partner that are necessary to function effectively. We believe that our concerns about clarifying the fact that equity ownership is not required and referencing the need for partner-equivalent authority to be consistent with Rule 2-01(f)(7)(ii)(B) might best be met, for example, by changing the words in paragraph 2 from:

"... may be a partner of the firm that issues the engagement report (or communicates an engagement conclusion, if no report is issued), another individual in the firm or an individual outside the firm. The engagement quality reviewer must be an associated person of a registered public accounting firm."

to:

“... may be any individual either in or outside the firm that issues the engagement report (or communicates an engagement conclusion, if no report is issued), who is an associated person of a registered public accounting firm, who possesses the equivalent professional authority of an equity owner in such firm, and who meets the other qualifications described in paragraph 3, below.”

As pointed out on page 9 of the Release, we note that the predecessor standard required that “the reviewer possesses knowledge of both relevant specialized industry practices and SEC rules and regulations in areas pertinent to the engagement but that the proposed standard, on the contrary, contains the less specific requirement only that reviewers “possess the level of knowledge and competence related to accounting, auditing, and financial or other reporting required to serve as the person who has overall responsibility for the same type of engagement.” However, we believe that to better assure that engagement quality reviews will add quality to audits as intended, the final standard should (a) set a minimum competence or experience level for reviewers that is clearly at a higher level than the minimum level that would ordinarily apply for assignment as the engagement partner for a similar engagement, and (b) provide more specific guidance in that regard than the general guidance that is currently available elsewhere, either in the competency standard contained in Ethics Interpretation 201-1 or in PCAOB Interim Quality Control Standard sec. QC 40.04-.08.

We point out that f/n 18 (also on p. 9) states, also quite broadly without specificity, that the “determination of what constitutes the appropriate level of knowledge and competence should be based on the circumstances of the engagement, including the size or complexity of the business.” Accordingly, we do not believe the objective stated on p. 9 in part B1 of the Release of establishing “more clearly the level of expertise and experience that is necessary to perform an objective engagement quality review” is likely to be met by the language in the proposed standard, and we believe this language in f/n 18 is so broad as to provide little or no assurance of consistent application and invites differences in judgment that are likely to cause disputes between firms and PCAOB inspectors.

While we do not believe the qualifications for reviewers set forth in the final standard should be so rigid and restrictive as to remove all need for judgment and tailoring to the circumstances, we nevertheless believe that references both to knowledge of SEC reporting requirements (possibly with some minimum experience levels stated) and to some minimal extent of any applicable specialized industry practices (clearly requiring less than demonstrated “expertise” or even prior experience with the industry but rather which could be obtained through the use of others to assist) should be reinstated from the predecessor to the final standard.

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

We believe that the final standard should both permit and encourage an informal, ongoing dialog between the engagement partner and the engagement quality reviewer in which advice and guidance of the reviewer is sought and given, for example, as to such matters as what will satisfy the reviewer’s requirements at the time his or her approval will be needed or what literature should be consulted to resolve a question. We believe such dialog would contribute to a higher quality audit with fewer back-end issues that result from “second-guessing” and tend to delay its completion, make the audit inefficient or worse, poses an unacceptable risk of compromise in the face of a deadline or a budgetary constraint. We believe that contributing to the overall quality of the audit should outweigh any competing concerns for protecting the objectivity of the reviewer.

Therefore, we believe the final standard should distinguish such informal dialog clearly from the activities that would otherwise be prohibited by the proposed language in paragraph 6 such as “supervise the engagement team.” Unless such dialog is permitted, subject to such an expressed distinction in the standard, it will be virtually impossible for auditors to comprehend how the reviewer’s approval could be reasonably assured when planning and conducting the audit thereby avoiding the back-end problems described in the preceding paragraph.

We also believe, however, that the engagement and engagement quality review objectives would best be met if more formal consultations with engagement quality reviewers continued to be permitted as they now are, provided proposed solutions are first developed and presented to the reviewer by other members of the engagement team for approval or revision such that the reviewer is not required to review and approve his or her own work.

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

We believe that paragraph 7-9 of the proposed standard adequately describe the appropriate scope of a typical engagement quality review. However, we have two comments about that:

- a. Paragraph 8j should be elevated to a higher position in the order presented such as between 8e and f, and
- b. Guidance setting forth the responsibilities of a lead reviewer to obtain communications from supporting reviewer(s) for circumstances when the engagement quality review is divided among several reviewers, for example, when multiple locations are involved, should be provided in the final standard.

A comment about paragraph 10 follows below under Question 7.

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 standard be changed?*

We believe the risk-based approach described in paragraphs 8 and 9 of the proposed standard, subject to our comments under Questions 4, 5 (item a), 8 and 9 herein, are appropriate.

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

We believe the guidance provided in paragraph 10 is adequate in all significant respects except that paragraph 10a should be expanded to include reference to “other documentation requirements of PCAOB standards relative to significant matters selected for review.”

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

We agree with the basic proposed requirement of paragraph 11 but believe that, as in the predecessor standard, the engagement quality reviewer's input and approval shortly after the engagement planning and strategy is relatively complete and in place, but before the bulk of the substantive auditing has begun should be more forcefully encouraged by the standard (without being required) particularly in certain designated circumstances (for example, for initial engagements or after a rotation of either the engagement partner or quality reviewer). This would afford better assurance that the significant risks of material misstatement are identified timely and that the major scope decisions will meet with the approval of the engagement quality reviewer at the end of the audit.

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

We have no problem with the proposed requirement of paragraph 12 to issue a concurring approval of issuance in accordance with Section 103 of the Act. However, we are seriously troubled by and object to the inclusion in the standard of the phrase “knows or should know.” Such a phrase resembles legal language used by adversaries to establish a case for negligence. It is inherently impossible for one to make a self-assessment as to what one

To: Office of the Secretary, Public Company Accounting Oversight Board
Re: PCAOB Rulemaking Docket Matter No. 025- Engagement Quality Review

April 28, 2008
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“should have known,” but to be nonetheless effectively required to do so by the operative standard might likely accomplish nothing more than (a) to help an adversary defeat a reviewer’s defense against civil or even criminal liability that is based on the good faith use of professional judgment, and (b) to establish a level of responsibility for the reviewer that exceeds that of the engagement partner in direct conflict with the statement to the contrary contained in paragraph 6 of the proposed standard. Moreover, the use of such language in the standard would be inconsistent with the risk-based principles inherent in the mandated approach to engagement quality reviews that effectively requires the reviewer to exercise his or her good faith professional judgment and is embodied in paragraphs 8-9 of the proposed standard.

Alternatively, we believe that, like its predecessor, the final standard should require that the reviewer’s conclusion supporting approval of issuance contain only negative assurance that is based on his or her direct representation of compliance with the standard as to scope and execution of the review.

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

We believe the documentation requirements outlined in paragraph 14 of the proposed standard are appropriate only if the final standard makes it clear that proposed requirement of paragraph 14c is intended only to call for broad, general descriptions of the procedures employed by the reviewer, such as those contained in paragraphs 8-10 and not by area or in the level of detail ordinarily expected for audit programs and other audit documentation.

In addition, the standard should clarify that the requirement in paragraph 14e may be met in the form of a standard conclusion (see our comments relative to Question 9, above) with exceptions and optional comments added if appropriate, and does not require any documentation of any specific or general deficiencies found that were corrected at the request of the reviewer prior to granting a concurring approval to issue the intended report or other communication.

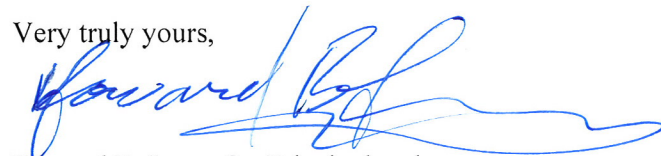
Question 11 – There is no question 11.

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

We do not believe any other documentation requirements of AS No. 3 should be expressly extended and made applicable to the engagement quality review. While we have no objection to paragraph 15 in the proposed standard, we believe it is entirely unnecessary as it would obviously apply.

Thank you for this opportunity to comment. We hope the Board finds our comments useful in its deliberations.

Very truly yours,



Howard B. Levy, Sr. Principal and
Director, Technical Services
Piercy Bowler Taylor & Kern,
Certified Public Accountants



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May 12, 2008

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

RE: PCAOB Rulemaking Docket No. 025, *Proposed Auditing Standard – Engagement Quality Review and Conforming Amendment to the Interim Quality Control Standards*

Dear Sir:

We appreciate the opportunity to respond to the Public Company Accounting Oversight Board's (PCAOB or the "Board") proposed auditing standard, *Engagement Quality Review* (the "standard" or "proposed standard") and conforming amendment to the interim quality control standards.

We strongly support auditing standards that promote audit quality and believe that a robust and effective engagement quality review that focuses on the significant judgments made and conclusions reached by the engagement team furthers that purpose. We support the Board's efforts to adopt an effective engagement quality review standard and acknowledge the Board's consideration of international auditing standards in developing the proposed standard. However, we believe that the proposed standard goes well beyond international auditing standards as promulgated by the International Auditing and Assurance Standards Board,¹ as well as the Board's current interim standard.² We believe that the Board's engagement quality review standard should be aligned with the international auditing standards. We are concerned that the additional effort and resulting cost will not have a commensurate benefit to audit quality.

We are also concerned about the absence of a clearly articulated objective for the review and significant aspects of the standard that, in our view, establish new and unwarranted standards of performance for engagement quality reviewers. In many respects, the proposed standard, in both substance and tone, seems designed to impose legal standards

¹ Proposed Redrafted ISA 220, *Quality Control for an Audit of Financial Statements* (ISA 220), and Proposed Redrafted ISQC 1, *Quality Control for Firms that Perform Audits and Reviews of Financial Statements, and Other Assurance and Related Services Engagements* were proposed in July 2007 and are scheduled to be considered for adoption by the International Auditing and Assurance Standards Board in September 2008.

² SECPS Requirements of Membership, Section 1000.08(f), *Concurring Partner Review of the Audit Report and the Financial Statements of Commission Registrants*.



of conduct on the engagement quality reviewer, as opposed to establishing standards to guide the engagement quality reviewer in performing an independent and objective review of the engagement team's audit work. As discussed in more detail below, we believe that the focus of the proposed standard will have significant unintended consequences.

We believe that our concerns should be addressed by more closely aligning the new standard with international standards, which we believe would create an appropriately focused and effective review standard. Moreover, this would also be consistent with the growing demand for convergence of worldwide accounting and auditing standards, and the broad-based recognition of the benefits of developing a single set of standards for worldwide use.

Objective of the Engagement Quality Review

We believe that the engagement quality review standard should set forth a clear objective for the review, which would appropriately focus the standard on audit quality. We believe that the following objective articulates the purpose of the standard:

The objective of the engagement quality review is to provide for an independent, objective review of significant auditing, accounting, and financial reporting matters, including significant judgments made and conclusions reached, that results in a conclusion about whether the engagement quality reviewer concurs with the issuance of an engagement report.

In our view, this language makes it clear that the standard requires a "review" of key matters. The standard should not aim to create an additional level of independent substantive auditing procedures or require the engagement quality reviewer to engage in substantive oversight of the audit engagement team, substantively evaluate the performance of the engagement team, or determine compliance with the audit documentation requirements. The level of effort associated with performing such an independent *evaluation* would significantly exceed that required in an independent *review* of significant judgments made and conclusions reached, and yet the incremental benefit from an independent evaluation would be marginal.

This proposed objective recognizes that the responsibilities of the engagement quality reviewer differ from those of the engagement partner. The engagement partner has overall and ultimate responsibility for the engagement and the engagement report. The engagement quality review is an element of quality control. As such, the reviewer is in a position to provide an objective review of significant auditing, accounting, and financial reporting matters, including significant judgments made and conclusions reached by the engagement team. But the engagement quality reviewer is not, and could not be as a practical matter, responsible for the audit. Unlike the engagement team, the engagement quality reviewer's access to client records is generally limited to the audit documentation and discussions with the engagement team; he or she generally has limited interaction with client personnel. These limitations preclude the reviewer from independently forming the



necessary judgments and conclusions that would be required for an independent evaluation of certain aspects of the engagement team's work.

The proposed objective is also consistent with the requirements of international auditing standards and would reduce divergence from such standards.

Requirements of the Engagement Quality Review

We believe that the following provisions of the proposed standard should be revised, as they depart significantly from the Board's interim standard and the international standards:

- Procedures that require the engagement quality reviewer to make "evaluations" or "determinations" that, without clarification, may be interpreted to require a level of effort that is similar to that required of the engagement team in performing the work itself and require more than a review of the engagement team's judgments and conclusions (paragraphs 7 and 8);
- The requirement that the engagement quality reviewer identify areas of "higher risk," regardless of materiality, for which the engagement team may have failed to obtain sufficient competent evidence or reached an inappropriate conclusion, rather than identifying risks of material misstatement of the financial statements or material weakness in internal control over financial reporting that may not have been identified by the engagement team (paragraph 9);
- The requirement that the engagement quality reviewer independently evaluate the adequacy of audit documentation, particularly its compliance with Auditing Standard No. 3, *Audit Documentation* (AS 3) (paragraph 10); and
- A new standard of performance for the engagement quality reviewer's work and a conclusion that departs from the negative assurance in the interim standard. The proposed standard would require the reviewer to affirmatively conclude that there is nothing the reviewer "knows or should know" that would preclude concurrence with the engagement team's issuance of the report (paragraph 12).

As discussed below, these provisions, as proposed, could impose substantial new burdens on the engagement quality reviewer without a commensurate benefit to audit quality.

The proposed standard seems to redirect the focus of the engagement quality reviewer away from the work of the engagement team to the work of the reviewer. That is, by creating new standards of performance for the reviewer and a "knows or should know" level of assurance, the provisions of the proposed standard become too focused on the adequacy of the engagement quality review itself, rather than on a proper assessment of the quality of the work performed by the engagement team. For example, instead of considering the judgments made by the engagement team, the reviewer would be required to perform sufficient work to have a basis for separately forming his or her own independent determinations (e.g., whether appropriate matters have been communicated to



the audit committee, whether there are areas that create a "higher risk" of non-compliance, and whether the engagement team complied with documentation standards, etc.).

By mandating that these separate determinations and judgments be made by the reviewer, the focus of the proposed standard becomes the reviewer's own basis for his or her determinations, rather than the reviewer's consideration of the judgments and conclusions reached by the engagement team. The judgments the reviewer makes will likely be seen as supplanting, rather than enhancing or confirming, those of the engagement team. We believe a focus on the reviewer's consideration of the judgments and conclusions reached by the engagement team provides for a more effective and efficient engagement quality review.

We believe that investors, issuers, and auditors should continue to expect engagement partners to make reasonable judgments. Engagement quality reviews contribute to audit quality and, along with the other quality control processes, combine to provide reasonable assurance about the effectiveness of the firm's system of quality control, as required. However, we see neither a purpose nor a benefit in redirecting the focus of the engagement quality review or in the additional costs that will undoubtedly be incurred to address the additional requirements.

The following sections explain in greater detail our concerns with particular provisions of the standard and set forth our recommended changes to the Board's proposal.

Scope of Review Procedures

Paragraphs 7 and 8 prescribe general standards and specific procedures for conducting the engagement quality review. While we generally agree with the nature of these procedures, we are recommending changes to paragraphs 7 and 8 (as set forth in Appendix B to this letter) to clarify which procedures will satisfy the reviewer's responsibility and to avoid any suggestion that the reviewer is required -- or indeed able -- to duplicate the work of the engagement team or make independent judgments about matters that are the responsibility of the engagement team.

These recommended changes provide a more appropriate scope of procedures to be performed by the reviewer. Specifically, these changes would clarify the expected level of work and avoid a fundamental change in the nature of the review function, which could otherwise compromise the important principles of objectivity underlying the standard. The standard should result in an engagement quality review that reinforces, not diffuses, the accountability of the engagement partner.

Engagement Quality Reviewer Risk Assessment

Paragraph 9 of the proposed standard requires the reviewer to identify areas within the engagement that pose a "higher risk" that the engagement team failed to obtain sufficient competent evidence or reached an inappropriate conclusion, rather than a requirement to identify areas that pose a "higher risk" of material misstatement of the financial statements.



Under the proposed standard, for the areas that pose such a "higher risk," the engagement quality reviewer would be required to evaluate whether the engagement team performed procedures that were responsive to those risks, whether the judgments made by the engagement team were reasonable in the circumstances, and whether the results of the procedures support the engagement team's overall conclusion.

We believe that it is important for the engagement quality reviewer to understand and review the significant risks of material misstatement to the financial statements and the risks of material weakness in internal control over financial reporting identified by the engagement team and the engagement team's response to such risks. However, we do not believe that requiring a separate assessment of the risk that the engagement team failed to obtain sufficient competent evidence or reached an inappropriate conclusion is practical or consistent with the objective of an engagement quality review for the following reasons:

- It is unclear how the engagement quality reviewer would make such a determination, particularly in hindsight. The standard does not articulate any procedures for making this determination, other than referring to the procedures in paragraphs 7 and 8 and "other relevant knowledge possessed by the engagement quality reviewer." In short, this concept of "higher risk," directed to the work of the engagement team rather than the financial statements or internal control over financial reporting, and without any reference to materiality, does not have any linkage to professional standards and we therefore do not believe it is subject to implementation in any reasonable or consistent manner.
- The Board's use of the term "higher risk" implies that there should always be some areas of higher risk, which presumably the reviewer must examine, even though there may be no audit areas that pose a sufficiently high risk to justify further consideration or action.
- The requirement seems to be more concerned with having the reviewer make his or her risk assessments separately from the engagement team, than with reviewing the engagement team's judgments for reasonableness. We question the focus of this requirement and the extent to which it will improve audit quality.
- We believe that paragraph 12, both as proposed and consistent with our recommended revision, contains provisions sufficient to prevent engagement quality reviewers from concurring with the issuance of the engagement report, if the reviewer believes that the engagement team failed to obtain sufficient competent evidence in accordance with PCAOB standards or reached an inappropriate conclusion about the subject matter of the engagement, based upon the engagement quality review procedures performed.

We recommend that the Board modify the proposed requirement in paragraph 9 to refocus it on whether certain important matters were identified during the engagement quality review that were not previously identified by the engagement team. These matters include



significant risks of material misstatement to the financial statements and significant difficult or contentious matters where consultation should be considered that were not identified by the engagement team. If such matters are determined to exist, the engagement quality reviewer should be required to communicate these matters to the engagement team and assess whether the engagement team responds appropriately. We believe that such a focus is much more likely to enhance audit quality.

As such, we recommend that paragraph 9 be replaced as follows:

9. Based on the procedures performed in accordance with paragraphs 7 and 8, and the engagement quality reviewer's knowledge, the engagement quality reviewer should assess whether any of the following matters were not previously identified by the engagement team:

- **significant risks of material misstatement to the financial statements,**
- **significant risks of material weakness in internal control over financial reporting, or**
- **significant difficult or contentious matters where consultation should be considered by the engagement team.**

If the engagement quality reviewer believes that there are such risks or matters, he or she should communicate that to the engagement team and then assess whether the engagement team has responded appropriately.

Review of Engagement Documentation

Paragraph 10 of the proposed standard requires the engagement quality reviewer to evaluate the engagement documentation. In particular, it requires the reviewer to evaluate whether the documentation "is appropriate in the circumstances and consistent" with AS 3.

Audit documentation is important and we support the Board's proposed requirement for an engagement quality reviewer to assess whether the engagement documentation supports the conclusions reached by the engagement team with respect to the matters reviewed by the engagement quality reviewer. However, as discussed below, we believe that the proposed standard, if not modified, would require a detailed, compliance-oriented review of documentation. We believe that the standard would impose substantial additional burdens on the engagement quality reviewer that would not enhance audit quality.

The requirements in paragraphs 9 and 10 of the proposed standard appear to duplicate certain other requirements of AS 3, and therefore, at a minimum, should be modified to avoid confusion. Paragraph 13 of AS 3 requires the engagement team to "identify all significant findings or issues in an engagement completion document." Paragraph 13 further states that "this document, along with any documents cross-referenced, should collectively be as specific as necessary in the circumstances for a reviewer to gain a thorough understanding of the significant findings or issues." In our view, the objective for the engagement quality review can be met by performing the procedures outlined in paragraphs 7 through 9 of the proposed standard, as amended by our proposed revisions,



which reflect existing requirements and include reading the engagement completion documentation.

Accordingly, while we concur with the Board's proposal that the requirement to review engagement documentation be limited to documentation that was reviewed in connection with the procedures required to be performed in accordance with paragraphs 7 through 9 of the proposed standard, we believe that the requirement to review engagement documentation should be further revised as follows:

- Omit the requirement to evaluate whether the audit documentation is consistent with AS 3. We do not believe that this specific requirement is consistent with the overall objective of the engagement quality review, nor do we think it will meaningfully enhance audit quality. The engagement partner has primary responsibility for compliance with AS 3. It should not be the engagement quality reviewer's responsibility to duplicate the engagement partner's work.
- Clarify that the purpose of the review of engagement documentation is to assess whether the documentation selected for review supports the judgments made and conclusions reached by the engagement team. Our recommended change would eliminate any implication that paragraph 10 creates a more general requirement to assess detailed matters that may not be within the scope of procedures set forth in paragraphs 7 through 9.

Accordingly, we recommend that paragraph 10 of the proposed standard be replaced as follows:

10. Engagement Documentation. Based upon the procedures performed in accordance with paragraphs 7, 8, and 9, the reviewer should assess whether the engagement documentation reviewed during the course of the engagement quality review supports the significant conclusions reached by the engagement team.

Concurring Approval of Issuance

Paragraph 12 of the proposed standard states that the engagement quality reviewer cannot provide "concurring approval" of the issuance of an engagement report if he or she "knows or should know" that any of four enumerated conditions exist. We believe that the engagement quality reviewer's concurrence is an important contribution to audit quality. We agree with the four enumerated conditions, which, if present, would preclude the engagement quality reviewer from concurring with the issuance of the engagement report. We also support the requirement that the engagement quality reviewer consider the knowledge obtained in performing the review in accordance with the proposed standard.

Nonetheless, we are very concerned by the potential implications of the inclusion of a "knows or should know" standard in paragraph 12. Whether or not the Board intended this consequence, we believe that this term fundamentally changes the basis upon which the reviewer can concur in the issuance of the report. Under the current interim standard, the reviewer can concur as long as "no matters had come to his or her attention that would



cause the [reviewer] to believe" that the financial statements did not conform to GAAP in all material respects or that the audit was not performed in accordance with GAAS. That is, "negative assurance" is the current standard of performance.

The proposed standard, by contrast, requires the reviewer, like the engagement partner, to determine whether he or she has sufficient grounds to positively concur with the issuance of the report. It converts the engagement quality reviewer's conclusion to one that requires an affirmative finding or representation that, by definition, must be based on the performance of sufficient procedures to support the finding or representation.

Further, the phrase "knows or should know" imports a legal formulation into an auditing standard. We believe that inclusion of this phrase in auditing standards is neither necessary nor appropriate. Auditing standards and legal standards are different. Auditing standards are designed to guide auditors in carrying out their audit responsibilities and to provide sufficient clarity so that auditors can understand the requirements of the standards and others can evaluate their performance.³ Legal standards, on the other hand, are rules intended to assess the legal significance of behavior and are often applied after the fact. How they are applied may vary based on various factors, such as forum, parties, applicable law, etc.

Moreover, auditors are largely unfamiliar with this type of legal terminology in the context of auditing standards. Unlike the current interim standard which includes the auditing language described above (i.e., "negative assurance"), inclusion of the proposed language would likely lead to misunderstanding and inconsistent application of the standard.

"Knows or should know," moreover, is a simple *negligence* standard,⁴ which we do not think is appropriate. In another context, the Securities and Exchange Commission (SEC) expressly declined to impose a standard of "mere" or "simple" negligence as a basis for disciplinary action against accountants as a result of violations of professional standards. In adopting revised Rule 102(e) in 1998, the SEC specifically recognized that "creating an undue fear that an isolated error in judgment would result in a 102(e) proceeding could be counterproductive," and rejected a simple negligence standard.⁵ We believe that the

³ We note that the requirement to exercise due professional care applies to the planning and performance of all audits and the preparation of reports pursuant to PCAOB and other auditing standards.

⁴ It is worth noting that on its face, the "should know" formulation does not make sense in the context of the proposed auditing standard. The phrase implies that an engagement quality reviewer will be able to determine what he or she "should know" (but does not know) at the time of deciding whether or not to concur. This reinforces the concern that the standard will govern not just the conclusion the reviewer must make in order to concur, but also post hoc scrutiny of the reasonableness of the engagement quality reviewer's judgment based on what he or she should have known.

⁵ Release No. 33-7593, *Final Rule: Amendment to Rule 102(e) of the Commissions Rules of Practice* (Oct. 19, 1998). The SEC limited the scope of Rule 102(e) to instances of reckless or highly unreasonable behavior (rather than instances of merely negligent behavior) and to patterns of repeated behavior indicating a lack of competence to practice before the Commission.



"knows or should know" standard raises similar concerns about the consequences of an isolated error of judgment by the engagement quality reviewer.

We believe that the proposed formulation for concurring approval will have unintended consequences. Referring to what the reviewer "knows, or should know based upon the requirements of this standard" implies that the reviewer must perform sufficient procedures under the requirements of the standard to "know" that the four specified conditions do not exist. This would likely lead engagement quality reviewers to engage in substantial procedures to conclude that they do not know that any of the specified conditions are present. The phrase "should know" necessarily creates a potential for post hoc questioning of whether an engagement quality reviewer should have identified a condition that would have precluded him or her from concurring with the issuance of the engagement report.

Coupled with most auditors' lack of familiarity with the "knows or should know" standard, we believe that engagement quality reviewers will be overly focused on being second-guessed as to what they should have known if a problem with the audit were later identified. Therefore, reviewers are likely to spend substantially more time performing additional procedures at a higher cost.

Accordingly, we recommend that the Board adopt a standard that omits the "knows or should know" formulation. We recommend that paragraph 12 of the proposed standard be revised to either conform to the language used in ISA 220,⁶ or alternatively, as follows:

12. The engagement quality reviewer must not provide concurring approval of concur with the issuance of an engagement report if, based on he or she knows, or should know based upon the requirements of his or her review in accordance with this standard, the reviewer believes that (1) the engagement team failed to obtain sufficient competent evidence in accordance with the standards of the PCAOB, (2) the engagement team reached an inappropriate overall conclusion on the subject matter of the engagement, (3) the firm's report, if a report is to be issued, is not appropriate in the circumstances, or (4) the firm is not independent of its client.

We believe that the proposed language retains the essence of the standard – that the reviewer cannot concur if he or she believes, based on the review, that any of the four enumerated conditions are present. However, it eliminates the inappropriate "knows or should know" standard, while promoting behavior that enhances audit quality.

Documentation of Engagement Quality Review Procedures

We believe that documentation is an important component of audit quality and of demonstrating compliance with the Board's auditing standards. Paragraph 14 of the proposed standard sets forth the documentation requirements for the engagement quality review. We believe that some aspects of paragraph 14 could result in significant

⁶ Paragraph 22(c) of ISA 220 requires the reviewer to document that "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."



divergence in implementation and substantial incremental effort. Specifically, certain of the documentation requirements, including paragraphs 14(d) and (e), are unclear.

For example, paragraph 14(d) requires the documentation to reflect when the procedures were performed. However, many of the procedures performed by the engagement quality reviewer are continuous and performed throughout the course of the audit. Accordingly, we believe that it would be impractical to document when the procedures were performed. In our view, we believe that it is more important for the engagement quality reviewer to document the date of completion of the procedures and concurrence with issuance of the engagement report.

We also note that paragraph 14(e) requires the auditor to document the results of the review procedures performed. We are concerned that this requirement is too vague and provides no guidance as to whether the "results" to which it refers are the same or are different from the "result" (i.e., concurring approval of issuance) referred to in paragraph 12. Moreover, to the extent that this requirement is intended to go beyond the requirements of paragraph 12, inclusion of this subparagraph could result in (1) a substantial increase in effort as compared to current practice under the PCAOB's interim standard and international standards, and (2) the need for a significant increase in engagement quality reviewer resources. We believe that these incremental efforts will yield minimal benefits to audit quality.

We recommend that the Board amend the proposed documentation requirements so that they are consistent with ISA 220, which generally requires documentation of the following:

- The procedures required by the standard have been performed
- The engagement quality review has been completed before the date of the auditor's report
- The reviewer is not aware of any unresolved matters that would cause the reviewer to believe that the significant judgments made and the conclusions reached were inappropriate.

Furthermore, we believe that the requirements of the standard, as amended, should supersede the documentation requirements of AS 3, as it relates to the engagement quality review (other than those provisions of AS 3 applicable to retention of and subsequent changes to audit documentation, as required by paragraph 15 of the proposed standard). In addition, the documentation requirements should provide flexibility in determining the method of documenting the results of the review, such as the use of review checklists or memoranda documenting the procedures performed.



Other Specific Provisions of the Proposal

In Appendix A to our letter, we have highlighted certain observations on several other provisions of the proposed standard that we believe merit further consideration by the Board.

* * * * *

We support the Board's continuing efforts to promulgate standards that promote and improve audit quality. As noted above, we believe that engagement quality reviews generally further that purpose because they provide an independent, objective pre-issuance review of the significant audit judgments made and conclusions reached. Our comments in this letter have been directed to those provisions of the proposed standard that we believe go beyond international standards and may result in significant increased costs for procedures that will likely not provide a commensurate improvement in audit quality.

We appreciate the opportunity to provide our perspective to the Board. We would be pleased to discuss our comments and to answer any questions that the PCAOB staff or the Board may have. Please contact Vincent Colman (973-236-5390) or Jorge Milo (973-236-4300) regarding our submission.

Sincerely,

A handwritten signature in cursive script that reads "PriceWaterhouseCoopers LLP".

Attachments



Proposed Auditing Standard – Engagement Quality Review
Comments on Other Specific Provisions of the Proposal

As indicated in our letter, this Appendix highlights observations on several other specific provisions of the proposed standard that we believe merit further consideration by the Board.

Effective Date

As proposed, the standard would be effective for reports issued on or after December 15, 2008. The proposed effective date would not permit sufficient time for registered public accounting firms to implement the new engagement quality review requirements. We also believe that the effective date should be linked to the beginning of an engagement period. By linking the effective date to the beginning of the engagement period rather than the report issuance date, the new requirements would (1) be known and anticipated as of the beginning of the engagement period, (2) allow the assigned engagement quality reviewer to comply with the requirements throughout engagement planning and execution, and (3) be in place for each quarterly review conducted under SAS No. 100, *Interim Financial Information*. In this manner, adoption of the new standard would be more effective and efficient.

The effective date should provide all registered public accounting firms with sufficient time to (1) adopt policies and procedures consistent with the new standard, (2) train their personnel in the requirements of the new standard, and (3) assign qualified engagement quality reviewers consistent with their system of quality control.

Engagements Subject to Engagement Quality Reviews

We support the Board's proposal that all registered public accounting firms – not just those that were members of the AICPA SEC Practice Section as of April 16, 2003 – be required to comply with the engagement quality review standard. We believe that requiring all firms to comply with the standard is consistent with the Board's directive under Section 103 of the Sarbanes-Oxley Act of 2002 and in the public interest.

As indicated in our letter, we believe that a standard on engagement quality review will enhance audit quality. However, while we acknowledge the Board's desire for the standard to apply to all engagements performed in accordance with the standards of the PCAOB, the requirements in the proposed standard appear to have been tailored to financial statement audits and integrated audits. Accordingly, it would be difficult to apply certain requirements to other types of engagements, such as attestations conducted in accordance with the Board's attestation standards, with appropriate consistency.

Furthermore, with respect to the evidence required to be assessed ("sufficient competent evidence") and the nature of the affirmative conclusion, the proposed standard appears to



place the engagement quality reviewer in a position of having to obtain as much or more evidence and, consequently, to provide a higher level of assurance, than even the engagement partner for certain engagements (e.g., a review of interim financial information or a comfort letter for underwriters). In addition, we believe that a requirement to apply an auditing standard to an engagement performed in accordance with attestation standards would result in confusion and inconsistent practice. We therefore believe that the standard cannot be practically applied to engagements other than financial statement audits and integrated audits. Accordingly, we believe that the standard should only apply to financial statement audits, integrated audits and, with improvement in clarity of how the standard should be implemented for reviews of interim financial information, to such interim reviews.

Qualifications of the Engagement Quality Reviewer

We agree with the Board that a competent and objective engagement quality reviewer is essential to an effective engagement quality review. Likewise, we agree that the determination of what constitutes the appropriate level of knowledge and competence should be based on the circumstances of the engagement, including the size or complexity of the business. However, we are concerned that the Board's use of an example from the oil and gas exploration industry in the release accompanying the proposed standard may, inappropriately, imply that an engagement quality reviewer should have a deeper level of industry expertise than necessary or required to function as an engagement quality reviewer, particularly in narrow or specialized industries.

In addition, we note that the proposed standard permits other individuals of the firm (i.e., non-partners) or individuals outside of the firm (subject to the competence, independence and other requirements of the proposed standard) to serve as engagement quality reviewers. Although we acknowledge that that this accommodation may facilitate implementation of the standard by smaller registered firms, we do not intend to change our existing practice of only having partners serving as engagement quality reviewers.

Communication between the Engagement Quality Reviewer and the Engagement Team

While we agree with the requirement of paragraph 5 of the proposed standard that the engagement quality reviewer must maintain objectivity, we also believe that communication and consultation with the engagement quality reviewer enhances audit quality.

Paragraph 5 of the proposed standard indicates that the engagement quality reviewer "must be independent of the company, perform the engagement quality review with integrity and maintain objectivity with respect to the engagement and the engagement team" (emphasis added). Paragraph 5 could be read to suggest that the PCAOB is changing the definition of the word "objectivity." Historically, objectivity has been defined with respect to the audit; that is, the engagement team and the engagement quality reviewer are required to perform their procedures with skepticism and objectivity. The requirement that the engagement



quality reviewer must maintain objectivity with respect to the engagement team could be misinterpreted to mean that the engagement quality reviewer is somehow limited in his or her ability to have discussions with the engagement team. We believe that such consultation is an important element of audit quality and that the standard should encourage consultation with the engagement quality reviewer.

To avoid the unintended consequence of limiting communications between the engagement team and the engagement quality reviewer, which we do not believe compromise objectivity, we recommend replacing the language in paragraph 5 with language similar to that of PCAOB interim standard, QC Section 20.09, so that it states the following: "Engagement quality reviewers must be independent of the company and perform all professional responsibilities with integrity, and maintain objectivity in discharging professional responsibilities."



Proposed Auditing Standard – Engagement Quality Review
Scope of Review Procedures

As indicated in our letter, we recommend that the Board revise the required procedures outlined in Paragraphs 7 and 8 of the proposed standard. We believe certain of the provisions in Paragraphs 8 could be clarified to provide more clarity about how to satisfy the presumptively mandatory requirements in each of these sections:

7. The engagement quality reviewer should evaluate ~~include an evaluation of the significant judgments made by the engagement team and the significant conclusions reached by the engagement team in forming the overall conclusion on in conducting~~ the engagement and in preparing the engagement report, if a report is to be issued. ~~To identify and evaluate the significant judgments and conclusions, The evaluation should be conducted by~~ the engagement quality reviewer ~~should include through~~ discussions with the person with overall responsibility for the engagement, discussions with other members of the engagement team as necessary ~~appropriate~~, and other procedures, as described in paragraphs 8 and 9.

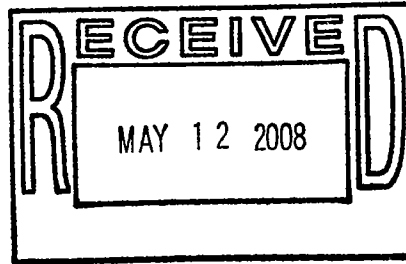
8. As part of performing the engagement quality review, the engagement quality reviewer should:

- a. **Obtain an understanding of the ~~firm's recent engagement experience with the company and~~ risks identified in connection with the firm's client acceptance and retention process for the company.**
- b. **Obtain an understanding of the company's business, significant activities during the current year, and significant financial reporting issues and risks through discussions with the person with overall responsibility for the engagement, discussions with other members of the engagement team, as appropriate, and the performance of the procedures enumerated in the subparagraphs below.**
- c. **Review the engagement team's evaluation of the firm's independence in relation to the engagement (i.e., the communication with the audit committee required by Rule 3526, *Communication with Audit Committees Concerning Independence*, formerly Independence Standards Board Standard No. 1, *Independence Discussions with Audit Committees*).**
- d. **~~Evaluate~~ Review engagement planning, including (1) the judgments made about materiality and the effect of those judgments on the engagement strategy and (2) the identification of significant risks, ~~including fraud risks of material misstatement to the financial statements and the risks of material weakness in internal control over financial reporting~~, and the plan for and performance of engagement procedures in response to those risks.**



- e. ~~Evaluate Review judgments made about (1) the materiality and disposition of corrected and uncorrected identified misstatements and (2) the severity and disposition of identified control deficiencies.~~
- f. ~~Determine if appropriate consultations have taken place on difficult or contentious matters. Review the documentation, including conclusions, of such consultations that have taken place on significant difficult or contentious matters.~~
- g. Read the financial statements, management's report on internal control over financial reporting, or other information that is the subject of the engagement and the engagement report (if an engagement report is to be issued) for the period covered by the engagement and for the prior comparative periods presented.
- h. Read other information in periodic filings and offering documents, as applicable, containing financial statements that are the subject of the engagement and are to be filed with the SEC and evaluate whether the engagement team has taken appropriate action with respect to material inconsistencies with the financial statements or material misstatements of fact of which the engagement quality reviewer is aware.
- i. ~~Determine if Review whether appropriate matters of which the engagement quality reviewer is aware have been communicated, or identified for communication to the audit committee, management, and other parties, such as regulatory bodies.~~
- j. Review the engagement completion document and confirm with the person with overall responsibility for the engagement that there are no significant unresolved matters.

Note: Matters of which the engagement reviewer is "aware" are those matters that have come to the attention of the reviewer during the course of performing the procedures required by this standard.



Hans E. Vanden Noort
Senior Vice President and
Chief Financial Officer

May 8, 2008

Office of the Secretary
PCAOB
1666 K Street NW
Washington, DC 20006-2803

Re: PCAOB Rulemaking Docket Matter No. 25

We appreciate the opportunity to provide our comments on the Public Company Accounting Oversight Board ("PCAOB") proposed auditing standard, *Engagement Quality Review* ("proposed standard").

We recognize the importance of an objective "second look" as a key element in ensuring audit quality. We also understand that PCAOB inspections have identified deficiencies in engagement quality reviews, and that obtaining cost-effective reviews has been challenging for some smaller registered public accounting firms. The PCAOB's Release indicates that the proposed standard aims to address these issues while avoiding unnecessary costs. However, we are concerned that certain provisions of the proposed standards would substantially increase audit costs without promoting better audit quality.

In our view, the current interim engagement quality review standards, based on the AICPA SEC Practice Section requirements for concurring reviews, are largely adequate. The larger registered public accounting firms already are performing most of the engagement quality review procedures included in the proposed standard by appropriately applying existing standards. Some of the proposed requirements in paragraphs 9 and 10 could be interpreted to require the engagement quality reviewer to re-perform detailed workpaper review and search for "missed risks" in the workpapers rather than objectively evaluate the quality of the engagement team's judgments on higher-risk areas, adequacy of procedures performed, documentation of key issues, and conclusions reached.

In addition, the "should know" threshold in paragraph 10 is open-ended regarding the quality reviewer's responsibilities to assess whether the engagement team failed to obtain sufficient, competent audit evidence in accordance with PCAOB standards. To avoid second guessing, many quality reviewers at the audit firms would likely interpret "should know" in the most restrictive way, and spend inordinate time on the review, adversely impacting public companies' audit fees. We believe this tendency for the firms to "practice defensive medicine" in costly and unintended ways was evident in the large accounting firms' approach to Section 404 testing under AS No. 2, prior to the clarified risk-based approach of AS No. 5. The firms' defensive interpretation of very prescriptive and open-ended audit rulemaking in that instance detracted from the very risk-based approach that the PCAOB intended.

Our concern extends to the more prescriptive requirements for documenting the engagement quality review in paragraph 14, items c. and e. (documenting the procedures performed by the reviewer and the results of the review). If interpreted to require extensive documentation along the lines of AS No. 3, this proposed requirement could add substantial time and cost to a review. We could envision a reviewer spending excessive time documenting all of his or her thoughts on the review and repeating matters included elsewhere in the workpapers. Reviewer time would be better spent in substantive discussions with the engagement team and objectively reviewing higher-risk issues. The reviewer should efficiently document the date of the review, key results and conclusions, and whether he or she concurred with issuance. The reviewer should be permitted judgment as to how much documentation is necessary, depending upon the risks and issues encountered.

Finally, we are troubled by the proposed standard's provisions to extend full engagement quality reviews to review engagements, attestation engagements and other engagements beyond audits of registrants' financial statements. The larger firms are already performing timely engagement reviews for quarterly Form 10-Q filings. We do not believe the additional costs of formal quality control reviews should be mandated for other engagements. The larger firms already have incentive and risk management protocols to address the needs for quality reviews on other engagements. Let the inspection process address those firms that have inadequate procedures rather than impose more costly standards across the board.

We understand that the PCAOB may need to issue a new engagement quality review standard to move beyond the current interim standards, to address the particular practice and resource issues of smaller firms, and to clarify expectations. However, we truly hope that any new standard recognizes the general adequacy of the existing standards for the larger firms, and avoids new provisions that will inevitably increase audit fees without a substantial improvement in audit quality. We feel that the feedback from the inspection process and ongoing PCAOB guidance to the firms would be the most cost effective way to address specific concerns about engagement quality reviews.

If you have any comments, please do not hesitate to contact me at (904) 357-9134.

Sincerely,



Hans E. Vanden Noort
Senior Vice President and
Chief Financial Officer



SCHOOL OF BUSINESS
University of Wisconsin-Madison

Larry E. Rittenberg

Ernst & Young Professor of Accounting & Information Systems

Ph: 608-262-2267; Email: lrittenberg@bus.wisc.edu

May 12, 2008

Office of the Secretary
PCAOB
1666K Street NW
Washington, DC 20006-2803

Re: Proposed Auditing Standard on ENGAGEMENT QUALITY REVIEW

Overview:

My perspectives are from the view of an academic who has spent my entire career with a career-long interest in auditing. I currently sit on two public company boards, one in China and one in the U.S. I understand the need for the PCAOB to issue guidance to ensure that there is consistent execution of the audit programs by partners and staff. A robust internal review of engagements for the quality of the audit performed should be helpful in meeting this overall objective. Thus, I am supportive of the PCAOB's efforts to improve audit quality.

At the most recent audit committee meeting of a U.S. Company on which I serve, the partner (from a Big 4 firm) presented a brief review of proposed PCAOB standards and how they might affect the audit. I was surprised to hear that they estimated that the engagement quality review standard would result in an increase of between 75 – 100 hours of partner time and additional costs of review (for \$1 billion revenue company).

The Audit Committee Chair questioned why the additional 75 – 100 hours was necessary when the firm had demonstrated to us that they had adequate processes to protect both the public and the audit committee, and that was a factor we considered when we changed auditors this year. My sense was that the standard was aimed at codifying best practices and I wondered if the firm was overreacting. The idea of ensuring that high quality audits are performed seems unassailable.

My understanding is that the PCAOB believes that many (but probably not all) firms need to improve their engagement review processes because the PCAOB inspection process uncovers too many audit deficiencies. The overall goal is to ensure high quality audits without adding disproportionately to the cost of audits.

Upon a second and third reading the proposed standard, I have developed some reservations about the current wording in the proposed standard. I have become concerned that the standard may have *some unintended consequences* of adding costs without adding (or contributing) to an increase in the quality of the audit. My sense, partially based on my reading of PCAOB inspection reports, is that there is a real need for consistent guidance for engagement reviews, but in particular for some of the smaller firms that audit public companies. I concur with the concern that many smaller public accounting firms have not demonstrated the expertise to fully implement concurring partner reviews, and some of the larger firms may not be sufficiently challenging the engagement partner. In my view, the addition of guidance for all firms is a good thing, and the firms must demonstrate that they are performing meaningful engagement quality reviews. Alternatively, if the firms cannot demonstrate meaningful engagement quality reviews, they should not be in the business of performing public company audits. Thus, there is a need for guidance. However, there is always a potential trade-off in becoming too prescriptive in a standard that may raise costs beyond that required to perform high quality engagement reviews.

I will first describe some overall concerns with the proposed standard and then will talk about specific paragraphs within the standard that may cause some problems. I will also address some of the specific questions you raise in your introduction to the standard.

Objective of the Guidance

I am concerned about the lack of a clear objective for the performance of the Engagement Quality Review. Let's assume that a public accounting firm has processes that are designed to ensure that all issues are properly documented and addressed in the audit engagement (a requirement under current standards). Then, I need to ask: What is the major purpose of the Engagement Quality Review? Is it:

1. To ensure that all of the required procedures have been performed, including documentation and resolution of high risk, or other significant areas, in the audit engagement, or
2. To require an independent, competent audit and accounting skeptic to evaluate the major decisions made by the engagement team, i.e. to exercise independent judgment as to whether the engagement team reached the correct solutions, as well as gathered appropriate evidence. In essence, this would be a 'super engagement partner' (at least one more independent level above the engagement partner).

I view these two objectives as being distinctly different. For example, paragraph 7 states that the review 'should include an evaluation of the significant judgments made by the engagement team and the conclusions reached ...'. This statement would imply that the objective of the standard is the second one listed above, i.e. a second evaluation of significant judgments. On the other hand, paragraph 10 covers the review of documents, and indicates that the review of documentation should address whether the documentation "indicates that the engagement team responded appropriately to matters that present a significant risk." Thus, paragraph 10 implies an Objective 1 noted above. Perhaps the standard intends to imply both, but if it does, you might want to consider timing issues. Further, we need to ask if this objective is necessary given that (a) it is the engagement partner's responsibility to see that documentation is adequate, and (b) a firm should have a formal internal review process to see that its auditors are adhering to professional (and firm) standards requiring adequate documentation.

I believe that the standard should be very clear that the objective is to ensure that there is an independent review by a knowledgeable person (or group) within the firm to ensure that a sufficient audit has taken place and that the financial statements reflect appropriate treatment of all material items in the financial statement. The ISA statement (footnote 8) implies objective no. 2 above. Does the PCAOB want both, or is objective 1 part of a normal quality review process that every firm should have, but is not required before the completion of the audit? That is a decision you will have to make based on more detailed information that you have from your inspection reports. Then, within the guidelines you present, I would leave it up to the firms to determine the most appropriate way to accomplish that objective.

One additional comment, if the objective is no. 1 above, we need to make sure that in this era of 'accelerated filings' and the pressure by the SEC to move the time deadline for audited filings to a quicker date after year-end, whether such a review can be completed before the deadlines to file such reports. Perhaps it can be addressed, as the standard describes, by more interim reviews of documentation by the engagement quality review team. My preference might be to leave objective no. 1 as part of the firm's internal review procedures to ensure quality audits.

Performance of the Engagement Quality Review

There is an implicit assumption that all of the review work is performed by **one person**, and that person must be an audit partner with a level of knowledge about a client that is equal to that of the engagement partner. However, I may be reading too much into the overall standard because a note to paragraph 5 does state that the reviewer “may seek assistance from others.” But, it does not specify the level (partner, manager, senior, etc.) from which that assistance may be procured. As I review the nature of the engagement quality review guidance proposed in the standard, it is my opinion that there is some work that could be reliably performed by someone other than a partner.

I will use an old example here. Back when I worked for Ernst & Ernst, they had a technical review committee in Detroit for the Detroit region. It was composed of partners, senior managers, and heavy seniors. They were experienced in auditing and accounting and very knowledgeable. Most of their reviews were of a technical nature, focusing on the 10K, but they also looked at the documented rationale of significant judgments made on an audit (for example, valuation of inventory or receivables). I found their reviews to be incredibly well done. The department was independent of the engagement partner, and they had the final word on whether the audit report could be issued. More importantly, the work could be reviewed at different levels, e.g. senior managers reviewing documentation, planning, and support for conclusions. Partners reviewed risk and major accounting or audit issues. A heavy senior might review aspects of documentation. It seems that such a model might work if the standard addresses both of the objectives noted above. However, the proposed standard does not seem to contemplate such a structure. I would allow the flexibility for a firm to determine the best way to accomplish the objective, rather than focusing on a ‘review partner’ approach. The engagement partner ultimately has a responsibility to determine that the audit was completed in accordance with PCAOB standards and the financial results are appropriate according to GAAP. The reviewing team should determine that there is sufficient support for that conclusion.

The introductory material in the proposed standard cites research by Epps and Messier. While I agree with the nature of their research, I am concerned that the standard may be implying that a “checklist or practice aid” may be required for all engagement reviews. While I do believe that many firms would benefit from such a practice aid, I also worry that we may contribute further to the checklist approach to auditing. Each firm should design their own procedures that best meet the objectives of quality review. A checklist may be useful, but so would other approaches that rely on more significant inquiry by the engagement team.

Other Comments

1. I am not sure why the standard is required for *reviews of interim financial information*. These engagements provide a different level of assurance than do the audit engagements. In my view, firms should develop their own internal quality processes that may, or may not, include an engagement quality reviewer for interim financial information.
2. There are a couple of issues in *paragraph 8* that might be improved:
 - a. I believe that in part b, the engagement quality reviewer should also obtain information about the quality of internal control, *as it had existed at the date of last report*, as important information to determine if the audit had been properly planned. Part 8(g) only seems to imply that the auditor look at the current report on internal control.
 - b. Part (f) implies that consultations take place on an engagement, but no criteria are given as to what is required for consultation. If it is judgmental, then the standard should so state. I am worried about this requirement because all of the firms will face continuing pressure to make more 'principles-based' decisions in the near future, and thus there will be a need to push more of the accounting analysis down to the engagement team. The key is to have processes in place, that could include consultation, that the engagement team gathers the correct information to make an informed and supportable accounting choice regarding the economic substance of transactions, or current states of value, and the client records them according to the appropriate GAAP.
3. Consistent with my comment earlier about the review process, I believe that *paragraph 10* could be spelled out a bit differently. The engagement audit partner and manager should determine that appropriate documentation is developed. There should be a process within a firm's audit methodology to demonstrate that such documentation has been developed. Thus, in my mind, the engagement reviewer (or team) should:
 - a. Determine that such a process to ensure that proper documentation exists, and there is evidence of that process in the working papers.
 - b. Then, assuming such a process exists, the engagement quality reviewer should sample existing documentation to determine that it meets the requirement. The sampling could be risk based, or on some other base that the PCAOB may think appropriate.

Further, the lead-in focuses on "engagement documentation of the matters that were subject to engagement quality review procedures". It is not clear what is meant by that phrase. Is it limited to the areas described in paragraph 8, or are there other criteria that may be applicable? Is it contemplated that there should be some random, or risk-based approach to examine audit evidence?

4. *Qualifications of the Engagement Quality Reviewer.* Para 4 on Competence may be difficult to clearly implement. For example, if an engagement partner is going to perform the engagement quality review of a company in a highly specialized industry, must that engagement reviewing partner have the same level of industry expertise as the engagement partner? This could cause some difficulty in areas such as oil and gas. The real issue, in my view, is whether the PCAOB expects to have the engagement review team utilize a review process to see that the audit is properly performed, or does it expect the engagement reviewing partner (or team) to have the level of expertise to fully understand all the risks applicable to that engagement, and to understand those risks at the same level as the engagement partner and engagement team, and thus be in a position to second guess the audit. The proposed wording, in my mind, assumes the latter. I think there should be consideration as to whether the former would be sufficient (my preference). I personally believe that a good reviewer, with knowledge of an industry, could do a sufficient engagement review, but not have all the same expertise as the engagement partner.

5. *Paragraph 12.* Let us assume that the purpose of the standard is to provide enough guidance such that the standard is adhered to by all firms that are registered to practice with the PCAOB. If that is the case, I don't believe we need the partial sentence that states: "or should know based upon the requirements of this standard. . .". That phrase introduces legal jargon into the auditing literature that could be dysfunctional. I believe such jargon is unnecessary because the presumption should always be that auditors will follow the standards.

Suggested Improvements

The following suggestions are intended to be constructive and address many of the issues raised in the introduction to the standard.

1. I would prefer a more *objectives-based* approach to the standard. If the objectives are more clearly laid out, the firms should be provided with flexibility to demonstrate that they are accomplishing the objectives (most likely within guidelines you further develop).

2. I prefer a change in *terms*. Rather than using the term "engagement quality reviewer", I suggest using a term that might recognize that an engagement quality review can be an individual partner, or could be a team that is led by an individual partner and might include other members. Such a term could be "engagement quality review team."

3. Given the objective of the engagement review process, it might be possible that the engagement quality review team might have more general expertise, such as expertise in reviewing the quality of audit engagements. This is in contrast to the detailed knowledge of the company being audited and the industry risks. That is not to say that I don't believe industry knowledge is necessary, but that knowledge may be pulled in by the engagement team and the engagement review process should determine that there is evidence that such knowledge was utilized in the audit.
4. The requirement for an engagement quality review should be eliminated for review reports on interim information. Since these reviews are not audits, and rely heavily on the quality of the company's internal control processes, I do not see the need for mandated engagement quality reviews.
5. An integrated audit requires an audit opinion on both the financial statements and the effectiveness of the company's internal control over financial reporting. I did not get the impression that these two issues are treated on an equal footing in the proposed standard (admittedly, I am probably biased here). I would suggest that issues related to internal control evaluations be elevated to the same level as the financial reports.
6. As noted earlier, the guidance on consultations could be improved. It is not clear when consultations are needed. It is usually a call by the engagement partner, or sometimes by the audit client, or there may be explicit guidance by each firm. It should be recognized that judgment is used in determining whether consultations are required and those judgments should be documented. Thus, the proposed guidance on consultations with the engagement review team could be placed in that context.

Responses to Specific Questions

1. *Overall objective.* Yes, I believe the standard definitely needs a more explicit objective statement.
2. *Requirement.* I believe it should be required only for audit engagements, and not for reviews of interim financial information. The level of assurance added by auditors in providing interim reviews is very different than that provided in connection with an audit.)
3. *Qualifications of Reviewer.* No, I do not believe the qualifications of the engagement quality reviewer are properly described. There are alternative ways to accomplish the objectives of an engagement quality review. Refer to comments above.

4. *Engagement team consultation with the engagement reviewer.* Each firm should have processes in place that determine when, and if, consultations with someone else in the firm should be performed. As stated in the views expressed above, I believe the purpose of this standard should be on the audit process that a firm has employed to conduct a high quality audit in accordance with the PCAOB standards. Thus it should not be necessary to consult with the engagement reviewer. However, I would stop short of prohibiting such a consultation. My major concern is that each firm should develop a process, and the engagement review team should focus on the audit process and the existence of support for conclusions reached by the engagement team, including an analysis of both accounting and internal control issues to support the audit opinions.
5. *Scope and Extent of the Engagement.* I do not believe they are appropriately described. Nor, do I believe they can be appropriately described until such time as the objective becomes clearer.
6. *Risk-based approach.* I believe the guidance is fine on this dimension. However, it is difficult to fully assess this question without better understanding the overall objectives of the proposed standard.
7. *Review of documentation.* The lead-in material that is described just before you ask question 7 seems clearer to me than the actual standard.
8. *Timing.* This seems fine.
9. *Standard for concurring approval.* I think this area can, and should be, improved. See my comments above.
10. *Documentation requirements for a review.* These seem appropriate.
11. *There was no question 11.*
12. *Relationship to AS3.* Yes, I believe the reference is appropriate.

Summary

Reading the proposed standard once again reminds me of how difficult the job of standard-setting is. Based on my reading of selected PCAOB inspection reports, there is a need for the proposed guidance. The guidance as to areas that should be reviewed, particularly in paragraph 8, is good. I do believe that there should be more emphasis in

specifying the objective of the standard, i.e. is it a review of the audit, or a second “guessing” of the audit by an experienced partner. I see these two as different.

While I am less concerned about the cost of the review process than some of my colleagues, I do believe that the cost considerations should be considered. If the same objective could be accomplished with different approaches, we should encourage firms to concentrate on the approaches that they can demonstrate (a) accomplishes the objectives of the standard, and (b) are most cost effective for them.

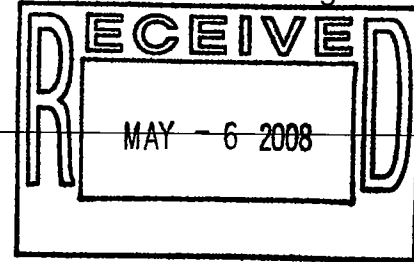
I would be happy to discuss any of the above observations at your convenience. I do applaud the PCAOB for moving forward in this important area.

Sincerely,

**Larry E
Rittenberg**

Digitally signed by Larry E Rittenberg
DN: cn=Larry E Rittenberg,
o=University of Wisconsin, ou,
email=lrittenberg@bus.wisc.edu, c=US
Date: 2008.05.12 10:11:31 -05'00'

Larry E. Rittenberg, PhD, CPA, CIA
Professor



April 30, 2008

Office of the Secretary
Public Company Accounting Oversight Board
1666 K Street N.W.
Washington, D.C. 20006-2803

**Re: 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**

Dear Sir or Madam:

Ross Stores, Inc. (“Ross” or the “Company”) is pleased to respond to the request for comment from the Public Company Accounting Oversight Board (the “PCAOB” or the “Board”) regarding Release No. 2008-002, *Proposed Auditing Standard – Engagement Quality Review and Conforming Amendment to the Board’s Interim Quality Control Standards*, PCAOB Rulemaking Docket Matter No. 025 (the “Release”).

We agree with the objectives of the Release—that through engagement quality review, audit firms will be able to identify and address audit deficiencies before concluding the audit. We understand that the PCAOB has considered information on this topic from PCAOB inspections and enforcement cases when formulating the proposed standard as well as standards in this area published by the International Auditing and Assurance Standards Board of the International Federation of Accountants and the Auditing Standards Board of the AICPA and from other forums.

Under the existing requirements, the concurring partner is required to review those significant auditing, accounting and financial reporting matters, discuss the engagement team’s identification and audit of high-risk transactions and balances, review documentation on the resolution of significant accounting, auditing and financial reporting matters, review the summary of unadjusted audit differences, read the financial statements and auditor’s report, and confirm with the engagement partner that there are no significant unresolved matters. This concurring partner review is required to be completed before the audit report is released.

The Release indicates that some members of the Board’s Standing Advisory Group believe that the existing requirements “did not provide for a thorough review to achieve the objectives of the requirement and that the reviews generally need to be more robust to provide investors with assurance on the quality of audit engagements.” Please consider the following:

- We believe the concurring review process currently used by our audit firm is sufficiently robust post-Sarbanes-Oxley and question whether the additional engagement quality review requirements would add value. We are also concerned that the incremental effort

and related cost of the review will not be commensurate with any added audit quality. We agree that the concurring partner's attention should center on higher-risk areas and believe the existing concurring partner review requirements already address this objective.

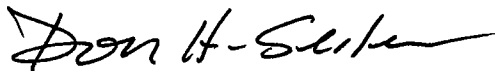
- We are concerned about the impact the additional reviews required by the auditing firm may have on the timing of the Company's earnings releases and regulatory filings. The Company adheres to tight deadlines in order to complete the internal controls over financial reporting and provide sufficient time for management, the independent auditors and the Audit Committee to fulfill their responsibilities of a large accelerated filer.
- We are also concerned with whether our audit firm has sufficient senior partner resources to enable them to meet all of the proposed requirements of engagement quality reviews for all of their public company clients on a timely basis.
- Finally, should this added regulation indeed move forward, we believe that a proposed implementation date for engagement reports issued on or after December 15, 2008 is too aggressive. We request providing a delay in the required effective date of the Release. We believe that the delay in the effective date will allow time for the public firms to address both implementation matters with their clients and resolve potential resource issues.

We appreciate this opportunity to comment, and would be pleased to discuss our letter with you further. If you have any questions or would like to discuss these issues further, please contact John G. Call, Senior Vice President, Chief Financial Officer at (925) 965-4315.

Very truly yours,



John G. Call
Senior Vice President, Chief Financial Officer
Ross Stores, Inc.



Donald H. Seiler
Chairman, the Audit Committee of the Board of Directors
Ross Stores, Inc.

cc: Mike Rudy – Deloitte & Touche



May 12, 2008

Office of the Secretary
PCAOB
1666 K Street, N.W.
Washington, DC 20006-2803

RE: Proposed Auditing Standard, *Engagement Quality Review*. PCAOB Release No. 2008-002.

To Whom It May Concern:

One of the expressed goals of the Texas Society of Certified Public Accountants (TSCPA) is to speak on behalf of its members when such action is in the best interest of its members and serves the cause of Certified Public Accountants in Texas, as well as the public interest. The TSCPA has established a Professional Standards Committee (PSC) to represent those interests on accounting and auditing issues. The PSC has been authorized by the TSCPA Board of Directors to submit comments on matters of interest to the committee membership. The views expressed in this letter have not been approved by the TSCPA Board of Directors and, therefore, should not be construed as representing the views or policy of the TSCPA.

We are delighted to have the opportunity to provide input into your deliberations regarding the Proposed Auditing Standard, *Engagement Quality Review*. We have structured our response to correspond to the questions posed in the Exposure Draft.

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?

We believe an objective should be stated in the Standard. Having an objective is consistent with the move towards principles-based guidance in the setting of professional standards. In developing the overall objective, we believe an engagement quality review should be designed to determine (1) if related financial statements are fairly presented in accordance with generally accepted accounting principles, (2) the internal control is adequate to produce materially reliable financial statements, and (3) the evidence gathered during the audit engagement provided adequate support for the audit opinion.

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 required?

We believe a quality review should be required for all engagements performed in accordance with the standards of the PCAOB. It should be made clear in the guidance that the scope and level of detail would vary based on the type of engagement being considered.

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

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In general, the qualifications for an engagement quality reviewer are appropriately described. However, we believe there are two areas in need of further clarification. First, the question of who is eligible to serve as a quality reviewer needs to be clarified. Second, the reviewer's "professional status in relation to that of the engagement partner" needs to be addressed. Our concerns about these two issues are noted below.

Under the Board's interim standard, the term used was "concurring partner" implying that the reviewer had to be a partner. The proposed standard states that the engagement quality reviewer may be "a partner or another individual in the firm, or an individual outside the firm." It appears the Board's intent is to base the qualifications of the reviewer on knowledge and experience, among other traits, rather than on the individual being a partner of the firm. If this is the Board's intent, we believe this fact should be specifically stated in the standard.

If the Board believes a non-partner could serve as the quality reviewer, it should take steps to caution accounting firms about the potential for objectivity problems. If a non-partner serves as a quality reviewer of a particular audit partner's engagement, that non-partner should not be allowed to be an engagement team member on another audit headed up by the partner for whom he/she performed the quality review. Such situations could result in a lack of objectivity on the part of the non-partner reviewer who knew he/she would receive a performance review from the partner on the other engagement.

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?

We believe the precautions noted in paragraphs 5 and 6 of the proposed standard are sufficient to allow the engagement team to consult with the engagement quality reviewer without impairing the reviewer's objectivity. However, we suggest that the Board consider adding a sentence, similar to the following, to the Note in paragraph 6: "The quality reviewer's objectivity would be considered to be impaired if the reviewer's comments in consultation with the engagement team could be construed as "direction" to the engagement team rather than mere consultation."

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?

We find the Board's descriptions of the scope and extent of engagement quality review procedures to be appropriate.

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 find the risk-based approach to the engagement quality review to be reasonable and we see no need to make any revisions.

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May 12, 2008
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Question 7: Are the proposed requirements for the review of the engagement team's documentation appropriate? If not, how should they be changed?

We believe the proposed requirements for the review of the engagement team's documentation to be very clear and in no need of revision.

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

We believe the information describing the timing of the engagement quality review is clear cut and should remain as presented.

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

We believe the standard for the engagement quality reviewer's concurring approval of issuance is appropriate.

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

We believe the documentation requirements are reasonable and appropriate and should not 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 believe the general standards of documentation and retention are the only ones that would appear to be applicable.

We appreciate the opportunity to provide our input to the standard-setting process.

Sincerely,

A handwritten signature in cursive script that reads "Sandra K. Johnigan".

Sandra K. Johnigan, CPA, CFE
Chair, Professional Standards Committee
Texas Society of Certified Public Accountants



12 May 2008

Our ref: ICAEW Rep 65/08

Office of the Secretary
PCAOB
1666 K Street,
N.W.
Washington
D. C. 20006-2803.

By email: *PCAOB Rulemaking Docket No. 025*

Dear Sir

**PCAOB RELEASE NO 2008- 002 PROPOSED AUDITING STANDARD:
ENGAGEMENT QUALITY REVIEWS**

The Institute of Chartered Accountants in England and Wales (the 'Institute') welcomes the opportunity to comment on the proposed auditing standard *Engagement Quality Review*.

The Institute operates under a Royal Charter, working in the public interest. Its regulation of its members, in particular its responsibilities in respect of auditors, is overseen by the Financial Reporting Council. As a world leading professional accountancy body, the Institute provides leadership and practical support to over 130,000 members in more than 140 countries, working with governments, regulators and industry in order to ensure the highest standards are maintained. The Institute is a founding member of the Global Accounting Alliance with over 700,000 members worldwide.

Our comments have been prepared with the help of our many members working around the world who have detailed knowledge and practical experience of US, EC and other regulatory regimes. We set out our main comments and answers to the PCAOB's specific questions below.

- 1. We are concerned by the introduction of a new standard of performance for Engagement Quality Reviewers (EQRs), requiring them to consider not merely what they know, but also what they 'should know'. This departure is critical and its effect should not be underestimated. We expect EQRs to significantly increase the scope and extent of their work to protect themselves, and for confusion to arise as to who is ultimately responsible for the audit opinion, We do not see additional value in these proposals and expect considerable increased cost to arise from this standard of performance, without corresponding benefit.**
- 2. The proposed implementation date makes the standard applicable for 2008 calendar-year end audits. This timetable is too aggressive since planning for many 2008 audits is already underway, involving EQRs in the review of planning. We recommend a more measured approach to implementation of the proposed standard.**



THE INSTITUTE
OF CHARTERED
ACCOUNTANTS

IN ENGLAND AND WALES

Please contact me should you wish to discuss any of the points raised in this response.

Yours sincerely

Katharine E Bagshaw FCA
Manager, Auditing Standards
ICAEW Audit and Assurance Faculty
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Main Comments

1 The role of EQRs and what they 'should have known'

Current requirements in both US GAAS and ISAs require the EQR to consider judgements presented to them by the engagement team. Furthermore, ISA 220 *Quality Control for Audits of Historical Financial Information* is currently being redrafted and proposes that the EQR's role is, among other things, to provide an objective evaluation of the significant judgments made by the engagement team, and the conclusions reached in formulating the auditor's report, emphasizing that it is the engagement team's determination of what is significant that sets the agenda for engagement quality review.

The proposed PCAOB standard departs significantly from current international practice since the EQR is directed not merely required to consider what is known, but also those matters the EQR 'should have known', possibly to levels approaching those currently applied by the engagement team, to avoid being second-guessed after the fact by those who have the benefit of hindsight, including PCAOB inspectors.

2 Timing of implementation

The proposed standard seeks implementation for 2008 calendar audits. This is unrealistic for a standard which cannot be approved by the SEC until relatively late in 2008 and raises the prospect of quality review work being performed under existing rules and then re-performed once the final standard is known. A more measured approach to implementing the new standard should be adopted.

3 Interaction between the engagement team and the EQR

The standard creates a requirement for the EQR to balance on the one hand a need to retain objectivity through separation from the engagement team, and by implication the audit client, and on the other hand to have a strong understanding of the issues involved in the audit. Very little is provided by way of guidance on how this balance should be achieved without compromising either objectivity or the quality of the review. We recommend that the PCAOB enhance the explanation of how EQRs can achieve such a balance. These proposals will also lead to confusion as to who has ultimate responsibility for the issuance of the audit opinion.

4 Applicability

We recommend that the PCAOB give further consideration to the applicability of this standard in three particular circumstances:

Foreign private issuer audits

PCAOB rules currently require certain review procedures to be made available to networked audit firms which are not members of the AICPA. This is commonly known as 'designated review' and focuses on the application of US accounting audit, disclosure and independence requirements where these are not the usual framework for the reporting audit firm. We are concerned that there is overlap between the role

of the EQR and the designated review. In the interests of efficiency, we recommend that the PCAOB consider and explain how these two requirements can fit together without creating unnecessary duplication.

Referred reporting engagements

Referred reporting engagements often involve the component auditor confirming that their work has been conducted in accordance with PCAOB standards. The introduction of the proposed standard would prompt the introduction of EQRs for component audits. However, in such circumstances, second-sight judgements are best provided by instructing offices rather than by involving new partners at the component level by the reporting office. We recommend that the proposed standard should not apply to component audits.

Non-audit assurance

The proposed standard seems drafted with audits in mind and we think that it would be difficult to comply with some of the requirements in a non-audit context, such as a review of interim financial information. We recommend that the PCAOB revisit this in finalising the standard and either provide additional guidance on application in non-audit contexts or specify that the standard solely applies to audits.

5 External sourcing of EQRs

We welcome the proposed standard's recognition that EQR arrangements can be sourced outside the firm. This is wholly beneficial for audit choice.

RESPONSES TO SPECIFIC QUESTIONS

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?

This standard should not state an objective. It is important that objectives in auditing standards are properly thought out within a proper framework, and that their role and status are crystal clear. While auditing standards are generally improved by the inclusion of a clear objective, the development of objectives on an *ad hoc* basis is not appropriate.

If an objective is considered necessary, the PCAOB should consider aligning it with the IAASB's proposed objective for their equivalent standard, ISQC 1:

The objective of the auditor is to obtain reasonable assurance that the audit complies with professional standards and regulatory and legal requirements, through the implementation of appropriate quality control procedures at the engagement level.

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 required?

No, as our comments above indicate.

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

We have not identified any particular problems with the description proposed, however, we recommend that the PCAOB consider whether its requirements in this area are significantly different to those required by the IAASB.

4. Should the proposed standard allow the engagement team to consult with the engagement quality reviewer during the engagement?

Yes, consultation should take place. Timely consultation is central to the role of the EQR. Further guidance on how this should occur would be welcome as our comments above indicate.

Would such consultation impair the reviewer's objectivity? The need for and benefits of consultation outweigh any potential actual or perceived impairment of the reviewer's objectivity.

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?

No, as our comments above indicate.

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?

No. The identification of significant engagement problems depends primarily on the quality of the *implementation* of the requirements of the standard. Requirements of standards alone cannot be expected to deliver audit quality. Adherence to the spirit, as well as the letter of the risk-based approach by both auditors and PCAOB inspectors will be necessary to achieve the desired outcomes.

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

No. The requirement for the EQR to consider what he or she 'should have known' is inappropriate as our comments above indicate.

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

We have not identified any particular problems with the timing proposed.

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

No. The proposed standard suffers from a lack of clarity as to who has ultimate responsibility for the issuance of the audit opinion. The standard should set out the

process for dealing with the rare circumstances in which the audit engagement partner and the EQR are unable to agree.

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

As drafted, the documentation requirements seem excessive, although the problem does not stem from the documentation requirement *per se*, but rather from the inappropriate requirements of the standard itself, as set out elsewhere in this letter. If the proposed standard is redrafted as suggested elsewhere in this letter, documentation problems will be less likely.

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 have not identified any other relevant provisions in AS No. 3.

CENTER FOR CAPITAL MARKETS COMPETITIVENESS
OF THE
UNITED STATES CHAMBER OF COMMERCE

DAVID T. HIRSCHMANN
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May 12, 2008

Mr. J. Gordon Seymour
General Counsel
Office of the Secretary and General Counsel
Public Company Accounting Oversight Board
1666 K Street, NW
Washington, DC 20006-2803

RE: Release No. 2008-002; Rulemaking Docket Matter No. 025
“Proposed Auditing Standard – Engagement Quality Review”

Dear Mr. Seymour:

The U.S. Chamber of Commerce is the world’s largest business federation, representing more than three million businesses and organizations of every size, sector, and region. The reliability and efficiency of the audit process is imperative to maintaining the competitiveness of our nation’s capital markets. We have been an advocate for the issuance of clear and effective auditing standards by the Public Company Accounting Oversight Board (“PCAOB”) and we appreciate the opportunity to comment on this proposed standard for engagement quality review.

Engagement quality review, conducted contemporaneously with the engagement, is an essential component of an effective audit process. This function was designated by Section 103 of the Sarbanes-Oxley Act of 2002 (“SOX”) as one of three areas for which the PCAOB should provide specific auditing standards. In April 2003, the PCAOB adopted its interim auditing standards which remain effective today, including a standard for conducting engagement quality reviews. Unfortunately, we are concerned that several aspects of the proposed standard are unclear and would result in unnecessarily expansive interpretations. Consequently, applying these vague provisions will result in a substantial increase in engagement quality review work and audit costs without a corresponding benefit to companies or investors.

First, the proposed standard does not state an overall objective of an engagement quality review. This is particularly troubling when considering that the

Mr. J. Gordon Seymour
May 12, 2008
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standard contains requirements that exceed international auditing standards and the PCAOB's current interim standard. We believe that modifications to the engagement quality review process should be supported by well-defined objectives and clear guidelines that focus on the most significant judgments made by an engagement team. Thus, the specific objectives sought to be achieved through this increase over current and similar standards should be clarified.

Second, paragraphs seven and eight of the proposed standard, which prescribe general standards and specific procedures for conducting the engagement quality review, in some instances suggest that the reviewer is required to duplicate the work of the engagement team or to make independent judgments about matters that are the responsibility of the engagement team. This would require new and independent evaluations by the engagement quality reviewer, rather than a review of evaluations that have already been made by the engagement team. For the engagement review process to remain efficient and effective it must focus on identifying material risks that the engagement team might not have identified. Therefore, the proposed standard should clarify that an engagement review should not consist of additional auditing procedures that are already the responsibility of the engagement team.

Third, the proposed standard identifies specific areas that the engagement quality reviewer must assess to provide concurring approval and increases the previous basis for concurring to a "knows or should know" standard. This will undoubtedly result in the performance of substantial new work due to the concern of engagement quality reviewers about being second-guessed as to what they "should have known." As was the case with Auditing Standard No. 2, before it was replaced with Auditing Standard No. 5, these additional procedures will increase costs without providing a corresponding benefit for investors relying on audit reports. Furthermore, this broadened standard – and potential increase in litigation risk – will likely result in smaller firms having difficulty engaging third parties to conduct engagement quality reviews. This may result in anti-competitive consequences contrary to the intentions of the PCAOB.

Fourth, the proposed standard requires that the engagement quality reviewer evaluate the engagement documents in accordance with the PCAOB's documentation standard, Auditing Standard No. 3. Under the current standards, compliance with this requirement is already the responsibility of the engagement partner. This extensive document review process would result in substantial additional work, which is

Mr. J. Gordon Seymour
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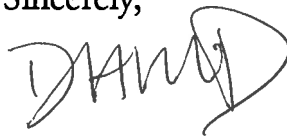
repetitive of work that is already required, and is not likely to enhance the overall quality of the audit engagement. These unnecessary increases in workload required under the proposed standard could also affect the issuer's ability to meet SEC filing deadlines.

Finally, the proposed standard requires the engagement quality reviewer to "maintain objectivity with respect to the engagement team." This vague requirement could be interpreted in a manner that would constrain the reviewer from engaging in constructive consultation with the engagement team. The information exchange between the reviewer and engagement team is an essential component of the audit process. Any limitations on this function would result in a deterioration of the quality of the overall auditing engagement.

The PCAOB has made commendable strides towards optimizing audit standards to ensure a sound and efficient audit process within the appropriate cost-benefit framework. Despite this progress, the provisions in this proposed audit standard will create inefficient and unnecessary requirements for the engagement quality review process. This will result in increased costs – for companies and their shareholders – that are highly disproportionate to any benefit that could be realized by investors or the broader business community.

Thank you for your consideration.

Sincerely,



David T. Hirschmann

cc: Hon. Mark W. Olson, Chairman, PCAOB
Hon. Daniel L. Goelzer, Member, PCAOB
Hon. Bill Gradison, Member, PCAOB
Hon. Charles D. Niemeier, Member, PCAOB



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

Enclosure 1

**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.”



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PROPOSED AUDITING STANDARD –)
)
 ENGAGEMENT QUALITY REVIEW) PCAOB Release No. 2009-001
) March 4, 2009
)
) PCAOB Rulemaking
) Docket Matter No. 025
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Summary: The Public Company Accounting Oversight Board (the "Board" or "PCAOB") is reproposing an auditing standard, *Engagement Quality Review*, that would be applicable to all registered firms and would supersede the Board's interim concurring partner review requirement.

Public
Comment: Interested persons may submit written comments to the Board. Such comments should be sent to the Office of the Secretary, PCAOB, 1666 K Street, N.W., Washington, D.C. 20006-2803. Comments also may be submitted by e-mail to comments@pcaobus.org or through the Board's Web site at www.pcaobus.org. All comments should refer to PCAOB Rulemaking Docket Matter No. 025 in the subject or reference line and should be received by the Board no later than 5:00 PM (EST) on April 20, 2009.

Board
Contacts: Gregory Scates, Deputy Chief Auditor (202/207-9114; scatesg@pcaobus.org) and Dmytro Andriyenko, Associate Chief Auditor (202/207-9130; andriyenkod@pcaobus.org).



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I. Introduction

Engagement quality review ("EQR") is an opportunity for the auditor to discover any significant engagement deficiencies before issuing its opinion. In an EQR, a qualified reviewer takes a fresh, objective look at the engagement, and, based on that review, evaluates whether it is appropriate for the firm to issue its report. A well-performed EQR can be an effective safeguard against erroneous or insufficiently supported audit opinions, and, accordingly, can contribute to audit quality and reduce the need for restatements.

In the 1970s, the audit profession began requiring EQR – known as "concurring partner review" – for some, but not all, engagements. The standard adopted by the profession applied to members of the Securities and Exchange Commission Practice Section ("SECPS") of the American Institute of Certified Public Accountants ("AICPA"), who were generally U.S.-based auditors of Securities and Exchange Commission ("SEC") registrants.

In 2002, Congress enacted the Sarbanes-Oxley Act (the "Act"), which created the Public Company Accounting Oversight Board ("the PCAOB" or "Board") and put in place a comprehensive, independent regulatory scheme for auditors of public companies. The Act directs the Board, among other things, to set standards for public company audits, including a requirement for each registered public accounting firm to "provide a concurring or second partner review and approval of [each] audit report (and other related information), and concurring approval in its issuance, by a qualified person (as prescribed by the Board) associated with the public accounting firm, other than the person in charge of the audit, or by an independent reviewer (as prescribed by the Board)."^{1/}

Soon after its creation, the Board adopted as its interim standards certain existing standards adopted and used by the auditing profession.^{2/} One such standard was the profession's concurring partner review requirement, which the Board continued to apply, on a transitional basis, to registered firms that were members of the SECPS.^{3/}

^{1/} Section 103(a)(2)(A)(ii) of the Act.

^{2/} PCAOB Release No. 2003-006, Establishment of Interim Professional Auditing Standards (April 18, 2003).

^{3/} See PCAOB Rule 3400T(b).



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According to this interim standard, "the concurring partner review . . . serves as an objective review of significant auditing, accounting, and financial reporting matters that come to the attention of the concurring partner reviewer and the resolution of such matters prior to the issuance of the firm's audit report with respect to financial statements of SEC engagements."^{4/} Registered firms that were not members of the SECPS – generally non-U.S. firms and some smaller firms – are not subject to this interim requirement.

On February 26, 2008, the Board proposed to replace the interim requirement with a new auditing standard, *Engagement Quality Review*.^{5/} The Board proposed this standard after considering feedback from its Standing Advisory Group ("SAG") as well as information from its inspection and enforcement programs. Some SAG members suggested that the interim requirement does not provide for a sufficiently thorough review to provide investors with assurance on the quality of engagements.^{6/} The Board generally agreed that new requirements are necessary to focus reviewers on the need to perform a robust review, rather than on whether particular matters had "come to [their] attention."^{7/}

Accordingly, the Board's proposal was intended to enhance the quality of the EQR process by strengthening the requirements in the standard. The Board believed that a more meaningful review would increase the likelihood that a registered firm would catch significant engagement deficiencies before issuing its audit report. At the same time, the Board recognized that an effective review need not – and should not – amount to a re-audit, and that the role of a reviewer differs significantly from that of an

^{4/} SECPS Requirements of Membership Sections 1000.08(f); 1000.39, Appendix E.

^{5/} PCAOB Release No. 2008-002, Proposed Auditing Standard – Engagement Quality Review and Conforming Amendment to the Board's Interim Quality Control Standards (February 26, 2008).

^{6/} The SAG discussed engagement quality review at its June 22, 2004 and October 5, 2005 meetings. Webcasts of those meetings are available on the Board's website at [www.pcaobus.org/News and Events/Webcasts Archive](http://www.pcaobus.org/News_and_Events/Webcasts_Archive).

^{7/} See SECPS Requirements of Membership Sections 1000.08(f); 1000.39, Appendix E.



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engagement partner. The Board's proposal therefore attempted to describe a review process that would effectively target areas of greatest risk while avoiding duplication of the engagement team's efforts.

The Board received 38 comment letters on its proposal.^{8/} A number of commenters commended the Board for proposing an auditing standard related to EQR, and noted that a well-performed engagement quality review is, in the words of one such commenter, a "pillar" of audit quality. Many commenters, however, were critical of key provisions of the proposal, including provisions describing the scope of the required review and the requirements for concurring in the issuance of the report.

The Board considered these comments and has made significant changes to the standard in response. At the same time, the Board continues to believe that in order to improve audit quality, the standard must require an EQR that serves as a meaningful way to identify significant engagement deficiencies in time to correct them. The Board also still believes that the new requirements should apply equally to – and be suitable for – all registered firms, rather than only a subset of them. For these reasons, the Board has determined that the interim requirement should be replaced. Because the Board has made extensive changes to the proposed standard, it is seeking comment on a revised standard.

II. Overview of the New Proposal

Like the original proposal, the standard that the Board is proposing is intended to strengthen the existing requirements for an EQR and lead to a more meaningful EQR process. Also like the original proposal, it would supersede the Board's interim concurring partner review requirement and apply equally to all registered firms. The significant refinements reflected in the new proposal result from a constructive public comment process and are intended to better tailor the standard to its purposes. As described in more detail below, the changes reflected in the new proposal are generally related to:

^{8/} Comments on the proposal are available on the Board's website at www.pcaobus.org/Rules/Docket_025.



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- *Applicability.* The new proposal would require an EQR for audits and reviews of interim financial information ("interim reviews"), but not for other engagements performed according to the standards of the PCAOB.
- *Objective.* The new proposal includes an explicit objective.
- *Reviewer qualifications.* Among other things, the Board refined the requirements in response to comments suggesting that only partners would have sufficient authority to conduct the review.
- *Scope.* Among other things, the Board revised the description of the procedures that would be required in an EQR, and, in recognition of the differences between an audit and an interim review, included separate requirements for reviewing those different types of engagements.
- *Concurring approval of issuance.* The Board revised the proposed provision on concurring approval by replacing the "knows, or should know based upon the requirements of this standard" formulation with a formulation grounded in the auditor's duty to exercise due professional care.
- *Documentation.* The Board clarified the scope of the documentation requirements.

The Board requests comment on the new proposal, including, in particular, the provisions that have been revised and responses to the specific questions below.

A. Applicability of the EQR Requirement

The Board's original proposal required an EQR for all engagements performed in accordance with the standards of the PCAOB. The proposed standard reflected the Board's belief that investors and other users of financial information expect that any engagement performed according to the Board's standards should be subject to an objective review by a qualified person outside of the engagement team. The release accompanying the original proposal explained that such engagements include integrated audits, audits of financials statements only, interim reviews, and other audit and attestation engagements.

A significant number of commenters expressed views on the applicability of the proposed standard to different types of engagements. None of the commenters



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objected to making the EQR mandatory for audit engagements, and the overwhelming majority of the commenters did not object to including interim reviews in the scope of the standard if the Board more clearly defined the requirements of an EQR for an interim review. While many of the commenters did not object to making an EQR mandatory for other engagements, some asked the Board to reconsider the practicality of having one standard for different types of engagements. As described below, after considering these comments, the Board is proposing to require an EQR for audits^{9/} and interim reviews – with separate requirements for each.

Applicability to Interim Reviews

Commenters noted that interim reviews are more limited in scope and have a different objective than audits. Therefore, they suggested, only a subset of the requirements set forth in the original proposal should be required for an EQR of an interim review. Commenters also recommended that the Board modify the requirements for providing concurring approval of issuance in an EQR of an interim review.^{10/} These commenters suggested that it would be inappropriate to require the reviewer to provide a higher level of assurance than what they termed the "negative assurance" required of the engagement team in an interim review.^{11/} According to commenters, if a higher level

^{9/} Section 103 of the Act directs the Board to include in its standards a requirement for an EQR of each audit report and concurring approval of issuance.

^{10/} Concurring approval of issuance is discussed below.

^{11/} An interim review does not provide the auditor with a basis to issue an opinion on the financial statements. Rather, as provided by Paragraph .07 of AU section ("sec.") 722, *Interim Financial Information*:

[t]he objective of a review of interim financial information . . . is to provide the accountant with a basis for communicating whether he or she is aware of any material modifications that should be made to the interim financial information for it to conform with generally accepted accounting principles. The objective of a review of interim financial information differs significantly from that of an audit conducted in accordance with generally accepted auditing standards Likewise, the auditor's responsibility as it relates to management's quarterly certifications on internal control over financial reporting is different from the auditor's responsibility as it relates to management's annual assessment of internal control over financial reporting. The auditor should perform limited procedures quarterly to provide a basis for determining whether he or she has



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of assurance were required in order to provide concurring approval of issuance, the reviewer would not be able to comply with the standard unless he or she performed procedures that were more extensive in scope than those required of the engagement team. For example, commenters suggested that the reviewer would not be able to determine the sufficiency of the evidence obtained because in an interim review the auditor is not required to corroborate management's responses with other evidence.^{12/}

The Board agrees with commenters who suggested that the EQR requirements for audits and interim reviews should be customized to reflect the differences in scope between these engagements. Accordingly, the new proposed standard includes specific requirements for audits and interim reviews in two separate sections, each of which describes review procedures and criteria for providing concurring approval of issuance. These provisions are discussed in more detail below, and should better align the EQR with the engagement under review.

Applicability to Other Engagements Performed According to PCAOB Standards

Some commenters suggested that the requirements of the original proposal were so specifically tailored to financial statement and integrated audits that it would be difficult to apply certain requirements to other types of engagements. For instance, some commenters questioned whether the requirement to obtain an understanding of significant financial reporting issues and risks would apply to a review of the assessment of compliance with servicing criteria under the SEC's Regulation AB. In the commenters' view, a requirement to apply an auditing standard to an engagement performed under attestation standards would result in confusion and inconsistent practice.

After considering these comments, the Board agrees that other engagements performed according to PCAOB standards are sufficiently different from audits and interim reviews, and that any EQR requirements related to such other engagements should be considered separately. Accordingly, the standard the Board is proposing would require an EQR only for audits and interim reviews. The two primary types of

become aware of any material modifications that, in the auditor's judgment, should be made to the disclosures about changes in internal control over financial reporting in order for the certifications to be accurate and to comply with the requirements of Section 302 of the Act.

^{12/} See AU sec. 722.07



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engagements excluded from the scope of the new proposal are engagements performed pursuant to Auditing Standard No. 4, *Reporting on Whether a Previously Reported Material Weakness Continues to Exist* and engagements required by the SEC's Regulation AB.^{13/}

Question:

1. Should the standard require an EQR for other kinds of engagements performed according to PCAOB standards? If so, what types of engagements should be included and what should an EQR of such engagements entail?

B. Objective of the Standard

In the release that accompanied the original proposal, the Board solicited comment on whether the standard should state an overall objective and, if so, what that objective should be. Most commenters expressed the view that the standard should contain a stated objective, and some commenters suggested an objective for the standard. Only three commenters believed that the standard did not need an overall objective.

The Board believes that a well-articulated objective can focus auditors on the purpose of a standard – the "big picture" – as they comply with the standard's more specific requirements and apply them to particular facts and circumstances. Applying a standard in light of its overall purpose should result in more effective and meaningful

^{13/} Under the SEC's Regulation AB and related rules (See Securities and Exchange Act Rule 13a-18, 17 C.F.R. § 240.13a-18; Item 1122 of Regulation AB, 17 C.F.R. § 229.1122), the annual report for a class of asset-backed securities must include from each party participating in the servicing function a report regarding its assessment of compliance with certain specified servicing criteria, and an attestation report by a registered public accounting firm on that assessment. The attestation report is to be prepared in accordance with standards for attestation engagements issued or adopted by the PCAOB.



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procedures and help auditors avoid a checklist approach. For these reasons, the Board included objectives in its recently proposed risk assessment standards.^{14/}

Based on commenters' feedback, the Board included in the new proposal an objective that is consistent with the specific requirements for performing an EQR and the requirements related to concurring approval of issuance. It is phrased as an objective for the engagement quality reviewer rather than as an objective of the process (the EQR), to emphasize the responsibilities placed on a reviewer by this proposed standard.

Questions:

2. Is the objective in the repropoed standard appropriately formulated? Does it articulate the purpose of an EQR?
3. Will this objective contribute to a more thoughtful and effective EQR?

C. Qualifications of the Engagement Quality Reviewer

In order to be effective, an EQR must be performed by a qualified reviewer. The Board's original proposal described the required qualifications of a reviewer in terms of the reviewer's competence, independence, integrity, and objectivity. Specifically, the original proposal:

- Required the reviewer to possess the level of knowledge and competence related to accounting, auditing, and financial or other reporting required to serve as the person who has overall responsibility for the same type of engagement;^{15/}
- Allowed the reviewer to be a partner or another individual in the firm, or an individual outside the firm;

^{14/} PCAOB Release No. 2008-006, Proposed Auditing Standards Related to the Auditor's Assessment of and Response to Risk and Conforming Amendments to PCAOB Standards (October 21, 2008).

^{15/} The release accompanying the original proposal noted that the determination of what constitutes the appropriate level of knowledge and competence should be based on the circumstances of the engagement, including the size or complexity of the company.



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- Required the reviewer to be independent of the company, perform the review with integrity, and maintain objectivity with respect to the engagement and the engagement team.

The original proposal also required the reviewer to be associated with a registered public accounting firm.

The release accompanying the original proposal sought comment on these proposed requirements and explained, among other things, how a qualified person not already associated with a registered firm could become associated with the firm issuing the report by performing the EQR. The proposed qualification provisions of the standard generated significant comment, and the Board has considered those comments. Commenters generally did not object to the requirement that the person performing the EQR be an associated person of a registered public accounting firm, and, because of the importance of that provision to the Board's ability to administer the standard, that provision has not changed in the new proposal. As described below, however, the Board is proposing some refinements to other aspects of the standard's qualification provisions in response to comments.

Competence

Many commenters agreed that the engagement quality reviewer should have a strong background in accounting, auditing and financial reporting. A number of commenters, however, believed that requiring the reviewer to have sufficient competence to serve as the engagement partner on the same type of engagement under review meant that the reviewer would have to be a "clone" of the engagement partner, which, they suggested, was not necessary for an effective EQR. Commenters were also concerned that this requirement placed too much emphasis on specialized industry expertise, which, they said, could limit unnecessarily the pool of suitable candidates and create resource constraints for firms.

At the same time, many commenters objected to the fact that the proposed standard did not expressly require the reviewer to be a partner. Others, however, believed that allowing someone other than a partner to perform the EQR would provide more flexibility to smaller and foreign firms. Commenters who suggested that the standard allow only partners to conduct the EQR were, for the most part, concerned that a non-partner would not have sufficient authority within the firm to provide an effective



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and objective review of the engagement partner's work.^{16/} In response to these comments, the Board is proposing certain changes.

The principles-based requirement in the original proposal for the reviewer to possess the level of knowledge and competence required to serve as the engagement partner in the same kind of engagement was intended, among other things, to make clear that under ordinary circumstances a non-partner in an accounting firm would be unqualified to conduct the EQR. Indeed, one commenter noted that a non-partner would be unlikely to have the experience or judgment of an engagement partner. At the same time, under the existing interim requirement, a firm may seek a waiver to engage an academic or other experienced accountant to perform the EQR.^{17/} Allowing a sufficiently qualified professor or other individual not employed by an accounting firm to perform the EQR should not negatively affect audit quality and may mitigate the compliance burden on sole practitioners and smaller firms. The Board intended the principles-based requirement to establish a sufficiently high standard for reviewer competence and authority, while providing sufficient flexibility for firms that wish to use reviewers who work outside a traditional partnership structure.

The Board continues to believe that this general competence standard is appropriate, and does not agree with commenters who suggested it requires the reviewer to possess skills identical to those of the engagement partner. The general competence provision merely sets a minimum requirement for those who would perform the EQR, but it does not require the reviewer's competence to match that of the engagement partner. In many cases, both individuals' competence will exceed the minimum level prescribed, but there is no requirement that they do so in tandem, or

^{16/} Some commenters also expressed concern that allowing someone who is not a "partner" to conduct the EQR would be inconsistent with the Act. The Board disagrees. Section 103(a)(2)(A)(ii) requires the Board to include in its auditing standards a requirement for "a concurring or second partner review and approval of such audit report (and other related information), and concurring approval in its issuance, *by a qualified person (as prescribed by the Board) associated with the public accounting firm, other than the person in charge of the audit, or by an independent reviewer (as prescribed by the Board).*" (Emphasis added). While that section describes the review as "a concurring or second partner review" – perhaps because those terms were already in use when the Act was enacted – it does not mandate that only "partners" conduct the review. To the contrary, the Board is specifically authorized to decide who is qualified to perform this review, so long as it is not the lead engagement partner.

^{17/} See PCAOB Rule 3400T.



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even at all. Moreover, the Board continues to believe that if industry knowledge is necessary to conduct a particular audit, it is similarly necessary to effectively review that audit. For these reasons, the general competence requirement in the new proposal is substantially the same as was originally proposed.

Although the Board believes that application of this requirement would rarely, if ever, allow a manager or other non-partner in an accounting firm to perform the EQR, it is sensitive to the concerns commenters raised about authority. While what constitutes authority is not easily defined, the Board believes that concerns about authority will most often arise when the reviewer is employed by the same firm as the engagement partner. Accordingly, the new standard explicitly requires a reviewer who is employed by the firm issuing the report to be a partner (or a person in an equivalent position). The Board recognizes that all partners in a firm do not possess the same authority, regardless of how that term is defined, but does not believe that imposing a requirement based on perceptions of authority among and between partners would be sufficiently clear to be workable. The Board therefore has attempted to address the authority issue through the proposed requirement that an in-house reviewer be a partner (or person in an equivalent position).^{18/}

Reviewers outside the firm would not be required to be partners because they may come from a variety of backgrounds. For example, they may be retired partners, professors of auditing, or other qualified accountants. In such circumstances, the Board believes that the general competence requirement – that the reviewer be qualified to serve as the engagement partner on the same type of engagement – should be sufficient to provide for an effective EQR.

Independence, Integrity, and Objectivity

The Board is also proposing revisions to the original proposal's provisions on objectivity in response to comments.^{19/} A number of commenters were concerned that

^{18/} A manager, for example, is not in a position equivalent to a partner.

^{19/} The new proposed standard, like the original proposal, requires the reviewer to perform the EQR with integrity and comply with all applicable independence requirements. Some commenters suggested that allowing a non-partner to serve as the reviewer would be inconsistent with SEC independence rules. Specifically, Rule 2-01(f)(7)(ii) of Regulation S-X defines "audit partner" to mean "a partner or persons in an equivalent position," and includes the "concurring or reviewing partner." The definition of "audit partner" is significant because "audit partners" (including "concurring partners")



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the original proposal could discourage communications between the reviewer and the engagement team, which, they said, would have a negative effect on audit quality.^{20/} Commenters believed that allowing the engagement team to consult with the reviewer would not impair the reviewer's objectivity and stated that such consultations are an important element of audit quality.

The original proposal described how a reviewer can maintain the necessary objectivity to perform an EQR – specifically, by not making decisions on behalf of, assuming any responsibilities of, or supervising the engagement team. A note to the original proposal stated that the engagement team may consult with the reviewer but that the reviewer should not participate in such consultations in a manner that would compromise his or her objectivity. Commenters believed that the language about objectivity in the note discouraged consultations.

In response to commenters' concerns, the Board has not included the note in the new proposal. The new proposal – like the original proposal – does not prohibit the engagement team from consulting with the reviewer. The Board agrees that such consultations may contribute to audit quality. Accordingly, reviewers may participate in such consultations, provided they do so in a manner that complies with the objectivity

are subject to certain independence requirements, such as mandatory partner rotation, 17 C.F.R. § 210.2-01(c)(6), and are members of the "audit engagement team," which is subject to other independence requirements. These definitions apply independence requirements to the person serving as the engagement quality reviewer, but they do not prohibit non-partners from performing that function. As described above, the Act gives the Board authority to determine who is qualified to perform the review. See *infra*, note 16. Moreover, under certain circumstances, a professor or other non-partner may perform the EQR even under the existing requirement. Accordingly, the Board will continue to consider anyone who performs the EQR to be an "audit partner" and a member of the "audit engagement team" for purposes of independence requirements.

^{20/} In particular, commenters expressed concern about the requirement in paragraph 5 that the reviewer "must . . . maintain objectivity with respect to . . . the engagement team;" the statement in the Note to paragraph 5 that "[p]ersonnel assisting the engagement quality reviewer also must be independent . . . and maintain objectivity with respect to the engagement and the engagement team;" and the statement in the Note to paragraph 6 that the reviewer "should not participate [in consultations with the engagement team] in a manner that would compromise his or her objectivity with regard to the engagement."



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requirements in paragraph 7 of the new proposal, which, with one clarification described below, are the same as those originally proposed. Because these requirements sufficiently describe how the reviewer may maintain objectivity, the note that appeared in the original proposal is unnecessary.

Also in response to comments, the Board has clarified paragraph 5 of the original proposal along with the accompanying note. That paragraph required the reviewer (as well as any assistants to the reviewer), among other things, to "maintain objectivity with respect to the engagement and the engagement team," which some commenters believed discouraged the reviewer from communicating with the engagement team. That was not the Board's intent, and, in fact, the reviewer must communicate with the engagement team in order to satisfy the requirements of the standard – as originally proposed and as re-proposed.

In order to better reflect the intent of the paragraph, the new proposal replaces the words "maintain objectivity with respect to the engagement and the engagement team," with "maintain objectivity in performing the review." In addition, the Board has also replaced the statement in the note that the "reviewer may seek assistance from others to perform the engagement quality review" with a statement that the "reviewer may use assistants in performing the engagement quality review." Some commenters understood the note to refer to members of the engagement team, which was not the Board's intent. The change should clarify that the note refers to the reviewer's assistants, who must also perform the review with objectivity.

As noted above, the original proposal provided that in order to maintain objectivity, the reviewer should not, among other things, supervise the engagement team. Some commenters interpreted this restriction to preclude partners with leadership responsibilities in a firm, region, service, or industry practice from reviewing any engagement performed by their subordinates in the firm, which, they argued, could unnecessarily strain resources. This was not the Board's intention. Accordingly, the Board has clarified the proposed standard by adding the words "with respect to the engagement subject to the engagement quality review" to the end of the prohibition (in paragraph 7 of the new proposal) on "supervis[ing] the engagement team." With this change, the new proposal better reflects the Board's intent.

Finally, some commenters suggested that the Board prohibit the engagement partner from serving as the reviewer of the same client's engagement for at least two years following his or her last year as the engagement partner, if he or she served as the engagement partner for less than five years – the maximum term allowed under the



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SEC's independence rules.^{21/} The Board agrees that the engagement partner should be prohibited from serving as the reviewer for at least two years following his or her last year as the audit engagement partner. As noted previously, in an EQR a reviewer is expected to take a fresh, objective look at the engagement. The Board believes that it would be harder for an engagement partner, who has had overall responsibility for the audit for a year or more, to perform the review with the level of objectivity of someone who is new to the engagement. Accordingly, the new proposal contains the restriction suggested by the commenters.

Questions:

4. Is it appropriate to explicitly require a reviewer from within the firm to be a partner or an individual in an equivalent position?
5. Should the standard allow qualified accountants who are not employed by an accounting firm to conduct the review?
6. Should the standard prohibit the engagement partner from serving as the reviewer for a period of time following his or her last year as the engagement partner? If so, is two years sufficient, or should it be extended?

D. EQR Process

In describing the scope of the review required under the original proposal, the Board attempted to balance the need for a rigorous review with the need to avoid requiring unnecessary or duplicative procedures. A scope that is too broad risks turning the EQR into a second audit and could impose unnecessary costs without achieving the purpose of an objective second look at work that was already performed. On the other hand, too narrow a scope could result in reviews that do not provide a safeguard against erroneous or insufficiently supported audit opinions.

Accordingly, the original proposal focused the EQR on those areas in the engagement that are likely to contain the greatest risk. It required an evaluation of the

^{21/} SEC independence rules do not prohibit the same person from serving as the engagement partner and engagement quality reviewer within one five-year term. See Rule 2-01(c)(6) of Regulation S-X, 17 C.F.R. § 210.2-01(c)(6). After serving a full five-year term, however, an engagement partner or engagement quality reviewer is subject to a five year "cooling off" period. Id.



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significant judgments made and conclusions reached by the engagement team, and specified certain procedures – some of which are similar to those described in the interim requirement and the standards of the International Auditing and Assurance Standards Board^{22/} – that the reviewer should always perform. The original proposal then required the reviewer to perform additional procedures in the areas within the engagement that pose a higher risk that the engagement team failed to obtain sufficient competent evidence or to reach an appropriate conclusion.

A significant number of commenters believed that the scope of the required EQR was so broad that it could amount to a re-audit. Commenters also expressed concern about the breadth of the requirement in paragraph 9 of the original proposal to perform additional procedures in areas of higher risk, and of the documentation review requirement in paragraph 10. The Board has considered these comments and is proposing changes.

Specifically Required Procedures

The original proposal described certain required procedures designed to focus the reviewer on the areas of the engagement that generally pose the greatest audit risk. These procedures required the reviewer to obtain an understanding about the firm's recent experience with the client as well as the client itself and to evaluate, among other things, the engagement team's audit planning, judgments about materiality, and identification of risks. The original proposal also required the reviewer to read certain relevant documents, such as the engagement report and the financial statements, and determine whether appropriate communications and consultations had taken place.

Commenters' concern was focused, for the most part, on the requirements to "[o]btain an understanding of the firm's recent engagement experience with the company and risks identified in connection with the firm's client acceptance and retention process," and "[o]btain an understanding of the company's business, significant activities during the current year, and significant financial reporting issues and risks."^{23/} Some commenters suggested that these provisions would require the

^{22/} ISA 220 (Redrafted), Quality Control for an Audit of Financial Statements, and ISQC 1 (Redrafted), Quality Control for Firms that Perform Audits and Reviews of Financial Statements, and Other Assurance and Related Services Engagements, issued in December 2008.

^{23/} Paragraphs 8.a and 8.b of the original proposal.



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reviewer to participate extensively in meetings with client management, make his or her own inquiries of client personnel, and perform other procedures that would duplicate work already performed by the engagement team. This was not the intent of the original proposal, and, to avoid confusion, the Board has made several changes that should clarify the scope of the requirements in the repropoed standard.

Like the original proposal, the new proposal requires the reviewer to evaluate the significant judgments made by the engagement team and the conclusions reached in forming the overall conclusion on the engagement and in preparing the engagement report and prescribes certain specific procedures. The new proposal makes clear (for both an EQR of an audit and an EQR of an interim review) that the reviewer should perform these procedures through discussions with the engagement team and the review of documents. This should clarify that the reviewer performs the EQR by reviewing the engagement team's work, rather than by auditing the company himself or herself.

The specifically required procedures are intended to give the reviewer the necessary information to evaluate the engagement team's significant judgments and conclusions, and, like all audit procedures, they must be performed with due professional care and professional skepticism. Accordingly, when performance of the procedures suggests a deficiency or red flag that, if pursued, could preclude the reviewer from providing concurring approval of issuance, the reviewer must follow up and make sure the matter is resolved before providing concurring approval.

The Board has also revised the requirements in the original proposal to "[o]btain an understanding of the firm's recent engagement experience with the company and risks identified in connection with the firm's client acceptance and retention process," and "[o]btain an understanding of the company's business, significant activities during the current year, and significant financial reporting issues and risks." In the new proposal, these requirements are elements of the requirement to evaluate engagement planning. In addition, they have been rephrased to direct the reviewer to evaluate the engagement team's consideration of these matters. These changes should clarify that the EQR is based on discussions with the engagement team and review of documents, rather than performance of procedures that should be performed by the engagement team.

As noted earlier in this release, the new proposal, in response to comments, describes specific requirements for an EQR of an interim review. These requirements are based on the proposed requirements for an EQR of an audit and are tailored to the different procedures performed in an interim review. Specifically, the evaluation of



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procedures performed by the engagement team, and information that the engagement quality reviewer is required to read has been modified to reflect the difference in scope between an audit and an interim review. For example, when performing an EQR of an interim review, the reviewer is not required to perform an evaluation of the engagement team's risk assessments and audit responses.

Additionally, when performing an EQR of an interim review – compared to an EQR of an audit – the reviewer is required, among other things, to –

- Read the "interim financial information for all periods presented and for the immediately preceding interim period," instead of the "financial statements;" and
- Read "management's disclosure for the period under review, if any, about changes in internal control over financial reporting," instead of "management's report on internal control."

Additional Procedures

After performing the specifically required procedures, the reviewer was required under the original proposal to "assess whether there are areas within the engagement that pose a higher risk that the engagement team has failed to obtain sufficient competent evidence or reached an inappropriate conclusion." For any such areas, the reviewer was required to evaluate whether the engagement team performed procedures that were responsive to the assessed risks, the judgments made by the engagement team were reasonable in the circumstances, and the results of the procedures support the engagement team's conclusion.

Some commenters were concerned that this provision was vague and duplicative of other provisions of the original proposal. Other commenters believed that the proposed additional procedures did not take into account materiality, and that performance of these procedures could divert the reviewer's attention from important matters such as the significant risks of material misstatement or material weakness in internal control over financial reporting.

The Board has reconsidered this provision in light of comments and determined not to include it in the new proposal. While the Board does not agree that this provision would focus reviewers on immaterial matters, it does believe, upon reconsideration, that the specifically required procedures are sufficient to focus the reviewer on the areas of high risk. In an EQR of an audit, the reviewer is required to evaluate the engagement



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team's risk assessments and procedures performed in response to significant risks,^{24/} including fraud risks. The new proposal highlights this requirement by stating it in a separate sub-paragraph. The reviewer is also required to review the engagement completion document and confirm with the engagement partner that there are no significant unresolved matters. A reviewer that performs the specifically required procedures in the new proposal with due professional care would necessarily focus his or her attention on the areas of greatest risk within the engagement.

Documentation Review Requirements

Finally, the Board believes that a reviewer will acquire a great deal of the information necessary for an effective EQR through a review of the engagement team's documentation of its work. Accordingly, the original proposal required the reviewer to evaluate whether the documentation of the matters subject to the EQR supported the conclusions reached, indicated that the engagement team responded appropriately to matters that present a significant risk, and met the documentation requirements of PCAOB Auditing Standard No. 3, *Audit Documentation* ("AS No. 3"). The requirement to review engagement documentation, under the original proposal, was intended to apply only to those areas that were subject to the EQR procedures. The scope of the documentation review requirement was, therefore, defined by the procedures required to be performed.

Some commenters believed that the documentation review requirements in paragraph 10 of the original proposal required a review of all or much of the engagement documentation. Some of these commenters believed that the phrase "matters that were subject to the engagement quality review" described all of the areas of an audit engagement because the entire engagement is subject to the EQR. Other commenters believed that the review of all or much of the engagement documentation would be necessary to determine whether the documentation supports "conclusions and representations in the engagement report." The commenters recommended that requirements to evaluate documentation be limited to the documentation that the

^{24/} The term "significant risk" is defined in the Board's recently proposed auditing standard on identifying and assessing risks of material misstatement to mean a "risk of material misstatement that is important enough to require special audit consideration." PCAOB Release No. 2008-006, Proposed Auditing Standards Related to the Auditor's Assessment of and Response to Risk and Conforming Amendments to PCAOB Standards (October 21, 2008). The Board intends that definition to apply to the EQR standard as well.



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engagement quality reviewer has selected for review in connection with the procedures required by the standard.

Additionally, several commenters believed that the requirement to evaluate the documentation for consistency with AS No. 3 goes beyond what should be required of the reviewer. These commenters suggested that the engagement partner has primary responsibility for compliance with AS No. 3, and that requiring the engagement quality reviewer to re-perform this work would not meaningfully enhance audit quality.

In response to the comments received, the Board has revised the documentation review requirements to clarify the extent of documentation that the engagement quality reviewer should review. In the new proposal, the Board replaced the phrase "documentation of the matters that were subject to the engagement quality review procedures" with "documentation that he or she reviewed when performing the procedures" required by paragraph 10, in an EQR of an audit, or 15, in an EQR of an interim review.^{25/} In addition, the new proposal requires the reviewer to evaluate whether such documentation supports "conclusions reached by the engagement team with respect to the matters reviewed" but not also "the conclusions and representations in the engagement report," as was required by the original proposal. Finally, the new proposal no longer requires the reviewer to evaluate the documentation for consistency with AS No. 3.

Questions:

7. Are the descriptions of the scope and extent of EQR procedures contained in the reproposed standard appropriate? Will the performance of these procedures result in a high-quality EQR? If not, how should these procedures be revised?
8. Are the specifically required procedures appropriately tailored to reflect the difference in scope between an audit and an interim review?
9. Do the specifically required procedures sufficiently focus the reviewer on areas of highest risk? Are there other procedures that should be required?

^{25/} Also to improve clarity, the new proposal requires the reviewer to evaluate whether the documentation of the matters reviewed indicates that the engagement team responded appropriately to "significant risks," rather than to "matters that present a significant risk."



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E. Concurring Approval of Issuance

The purpose of the required procedures in an EQR is to provide the reviewer with a sufficient basis to make a meaningful decision about whether to concur in the issuance of the audit report.^{26/} That decision must be based upon knowledge about the engagement obtained through performance of the standard's requirements, but concurring approval of issuance is not a second opinion, and the reviewer does not need to perform a second audit in order to provide it. The original proposal attempted to articulate this distinction in the standard that must be met in order for the reviewer to provide concurring approval of issuance. Specifically, the original proposal provided that the reviewer must not provide concurring approval of issuance if he or she knows, or should know based upon the requirements of the standard, that (1) the engagement team failed to obtain sufficient competent evidence in accordance with the standards of the PCAOB, (2) the engagement team reached an inappropriate overall conclusion on the subject matter of the engagement, (3) the firm's report, if a report is to be issued, is not appropriate in the circumstances, or (4) the firm is not independent of its client.^{27/}

A substantial number of commenters objected to this proposed provision and were most concerned about the standard's use of the phrase "knows, or should know based upon the requirements of this standard." Some objected to the inclusion of what they called "legal language" in the Board's standard and claimed that the proposed provision would change the nature of the reviewer's conclusion from "negative assurance" to "positive assurance." Others were concerned that the provision would be unworkable because, as stated by one commenter, it is inherently impossible to make a self-assessment of what one "should have known." Similarly, some commenters believed that the proposed provision would, in effect, require the reviewer to serve as a second engagement partner. Finally, some commenters suggested that the "should know" part of the formulation would create a potential for *post hoc* questioning with the benefit of hindsight – or "second guessing" – about whether a reviewer should have identified a condition that would have precluded him or her from providing concurring approval of issuance.

Commenters who opposed the proposed provision generally did not object to the list of the conditions that would preclude the reviewer from providing concurring

^{26/} The Act requires the Board's standard to provide for concurring approval of issuance of each audit report. See Section 103(a)(2)(A)(ii) of the Act.

^{27/} Paragraph 12 of the original proposal.



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approval of issuance. These commenters recommended requiring the reviewer's conclusion to be based on what he or she actually knows about the engagement, having performed the review in accordance with the provisions of the standard, rather than on what he or she should know. One such commenter recommended the Board rely on the concepts of due professional care, professional judgment, and lack of recklessness, which, the commenter said, are already included in the professional literature in describing the reviewer's responsibilities.

A small number of commenters approved of the original proposal's provision on concurring approval of issuance. One such commenter noted that it "requires the reviewer to make inquiries into the audit" and stated that "[t]his modest duty of inquiry is critical to making the engagement quality review something more than a 'hear no evil, speak no evil' exercise." Other supporters of the proposed provision suggested that it would further legitimize the EQR process.

The Board continues to believe that the existing standard's description of the requirements for providing concurring approval of issuance is inadequate and that a new provision is necessary. The Board also believes that a new EQR standard should explicitly include a standard of care, particularly in light of some of the comments it received on the original proposal. The Board recognizes that the original proposal suggested to some commenters that the Board would evaluate decisions to provide concurring approval of issuance with the benefit of hindsight. Moreover, the Board understands that such concerns may be particularly acute in the context of an EQR, which involves reviewing someone else's work and then concurring in the firm's opinion.

Accordingly, the Board has determined to revise the formulation of the standard for concurring approval in its repropoed standard. The revised provision would rely on the existing concept of due professional care, rather than the original proposal's "knows, or should know based upon the requirements of this standard" formulation. Specifically, for an EQR of an audit, the new proposal provides that the reviewer "may provide concurring approval of issuance only if, after performing with due professional care the review required by this standard, he or she is not aware of a significant engagement deficiency." A note to the same paragraph describes a "significant engagement deficiency" as any of the same four conditions included in the original proposal's provision on concurring approval of issuance.^{28/} The new proposal's requirements for

^{28/} As included in the new proposal, these conditions are: (1) the engagement team failed to obtain sufficient appropriate evidence in accordance with the standards of the PCAOB; (2) the engagement team reached an inappropriate overall conclusion on the subject matter of the engagement; (3) the engagement report is not appropriate in



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providing concurring approval of issuance in an EQR of an interim review are the same, except that the Board has modified the first of these four conditions in light of the differences between an interim review and an audit. Specifically, in an EQR of an interim review, the first condition is "the engagement team failed to perform interim review procedures necessary in the circumstances of the engagement" rather than "the engagement team failed to obtain sufficient appropriate evidence in accordance with the standards of the PCAOB."

Auditors have an existing duty to perform their work with "due professional care."^{29/} The auditing standards describe "due professional care" as "reasonable care and diligence" and note that negligent performance of audit procedures violates the due professional care requirement.^{30/} The SEC has recognized that, like all other audit procedures, the engagement quality review must be performed with "due professional care"^{31/} – a position that has been upheld by a federal court of appeals.^{32/}

the circumstances; or (4) the firm is not independent of its client. In order to be consistent with the Board's proposed standards on risk assessment, the new proposal refers to "sufficient appropriate" rather than "sufficient competent" evidence.

^{29/} AU sec. 230, *Due Professional Care in the Performance of Work*.

^{30/} See AU sec. 230.05; AU sec. 230.03, quoting Cooley on Torts (4th ed. 1932) ("he undertakes for good faith and integrity, but not for infallibility, and he is liable to his employer for negligence, bad faith, or dishonesty, but not for losses consequent upon pure errors of judgment").

^{31/} See, e.g., In the Matter of Robert D. Potts, 53 SEC 187, 195-97 (September 24, 1997).

^{32/} See Potts v. SEC, 151 F.3d 810, 813 (8th Cir. 1998), cert. denied, 526 U.S. 1097 (1999) ("Having taken on the concurring review task, Potts also shouldered the duty to perform that task professionally Accordingly, we reject the view put forward by the AICPA that a concurring partner is not an auditor and thus not subject to GAAS."). The AICPA SECPS revised its concurring partner review standard after the Potts case. The revisions did not alter the requirement to perform the review with due professional care.



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While auditors should be more familiar with "due professional care" than the concurring approval standard in the original proposal, the requirement to exercise due professional care imposes on a reviewer essentially the same requirement as the "knows, or should know based on the requirements of this standard" formulation in the Board's original proposal. To perform an EQR with due professional care, a reviewer must undertake the required procedures with "reasonable care and diligence."^{33/} A reviewer therefore would be expected to know the things that a reasonably careful and diligent EQR would uncover. Accordingly, under the revised standard, like the one originally proposed, a reviewer cannot evade responsibility because, as a result of an inadequate review, he or she did not discover a problem that a reasonably careful and diligent review would have revealed. At the same time, eliminating the phrase "should know" from the repropoed standard should alleviate commenters' concerns that the Board would evaluate decisions to provide concurring approval of issuance with the benefit of hindsight.

Question:

10. Is the standard for the engagement quality reviewer's concurring approval of issuance appropriately described in the repropoed standard? Is the first condition appropriately tailored to reflect the difference in scope between an audit and an interim review?

F. Documentation of the EQR

In the release accompanying the original proposal, the Board noted that the information received from PCAOB inspection teams, findings from PCAOB enforcement cases, and recent academic research indicated deficiencies in the documentation of concurring partner reviews prepared in accordance with the Board's interim requirements. In some cases, these deficiencies prevented a determination by PCAOB inspectors as to whether the scope of the review was appropriate, and may have contributed to the firm's failure to properly address the concurring partner's findings. The academic research showed substantial variability and lack of detail in the documentation of concurring partner reviews.

In order to address these problems, the original proposal contained more specific requirements related to the documentation of the EQR than the Board's interim

^{33/} See AU sec. 230.05.



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standard.^{34/} The original proposal provided that the engagement documentation should indicate: who performed the review; the areas of the engagement subject to the review; the procedures performed by the reviewer; when the review procedures were performed; the results of the review procedures; and whether the engagement quality reviewer provided concurring approval of issuance. Additionally, the requirements in AS No. 3 related to retention of and subsequent changes to audit documentation would also apply to the documentation of the EQR.^{35/}

A number of commenters viewed the requirements of the original proposal as unnecessarily burdensome. Some of the commenters suggested that the original proposal would require the reviewer to document information concerning all areas of the engagement since all areas of the engagement could be subject to the EQR. Other commenters were concerned that detailed documentation of the EQR procedures and their results, which would be duplicative of the engagement team's efforts, would be required under the original proposal. Most commenters recommended that the Board clarify the proposed requirements in order to avoid excessive documentation related to the EQR.

After considering these comments, the Board continues to believe that the documentation requirements in the new standard should be more specific than those in the Board's interim standard. As discussed above, poor documentation has not only made it difficult for the Board's inspectors to evaluate whether an EQR was appropriately performed, it may have also contributed to the firm's failure to properly address the reviewer's findings. The Board has, however, attempted to clarify the proposed requirements to avoid duplication of effort. Specifically, in the new proposal the Board has replaced the broad requirements to document "the areas of the

^{34/} Under the interim standard, "[t]he engagement files should contain evidence that the firm's policies and procedures with respect to the concurring partner review requirement were complied with before the issuance of the firm's audit report. Ordinarily, this would include documentation that the concurring partner reviewer has performed the procedures specified by the firm's policies and that no matters that have come to the attention of the concurring partner reviewer would cause him or her to believe that the financial statements are not in conformity with generally accepted accounting principles in all material respects or that the firm's audit was not performed in accordance with generally accepted auditing standards."

^{35/} Commenters did not object to applying these requirements of AS No. 3 to the documentation of the EQR.



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engagement subject to" the review, the procedures performed by the reviewer, and the results of those procedures with more narrowly tailored requirements, the scope of which should be clearer.

Under the new proposal, the documentation should "contain sufficient information to identify" who performed the review, the documents reviewed and significant discussions held during the review,^{36/} and the date that the reviewer provided concurring approval of issuance. If the reviewer did not provide concurring approval of issuance, the new proposal would require documentation of the reviewer's reasons for not providing concurring approval of issuance. These requirements should not be unduly burdensome or distract the reviewer from his or her task to identify any significant engagement deficiencies so that they may be corrected. At the same time, they should be sufficient to allow both the Board and the firm itself to understand how the review was conducted and how significant issues were resolved.

Question:

11. Are the documentation requirements in the repropoed standard appropriate? If not, how should they be changed?

G. Timing of the EQR

The Board noted in the release accompanying the original proposal that the EQR could be more effective if performed shortly after the engagement team's resolution of significant issues. Accordingly, the original proposal required the reviewer to complete the EQR prior to providing concurring approval of issuance but stated, in a note, that the EQR procedures may be performed at various points throughout the engagement.^{37/} Most of those who commented on this issue believed the description of the timing of the review in the original proposal was appropriate. In particular, several commenters were in favor of allowing the reviewer to perform the review at various points throughout the engagement.

The Board continues to believe that, as long as the review is completed before concurring approval of issuance is provided, the reviewer and the engagement team

^{36/} Significant discussions are those that the reviewer will rely upon to demonstrate compliance with the standard.

^{37/} Paragraph 11 of the original proposal.



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should determine the appropriate timing for the review procedures. In the new proposal, the requirement to complete the review before providing concurring approval of issuance is explicitly included in the paragraphs on concurring approval, rather than in a separate provision on timing of the review.^{38/} Accordingly, the new proposal does not include a statement explicitly allowing the reviewer to perform procedures at various points during the engagement. Such a statement is not necessary because the new proposal – like the original one – does not impose any requirements on when the review take place, other than that it be completed before the reviewer provides concurring approval of issuance.^{39/}

H. Effective Date

The Board originally proposed to make the standard effective, subject to approval by the SEC, for engagement reports issued (or the communication of an engagement conclusion, if no report is issued) on or after December 15, 2008. Commenters expressed concern that this effective date would not allow sufficient time for registered firms to implement the new requirements. Many commenters noted that an engagement quality reviewer is typically selected early in the engagement process so that he or she can review the engagement planning activities and interim reviews, and that audits of some issuers with fiscal years ending December 31, 2008 had already advanced beyond the planning stage. The EQRs on these engagements, the commenters suggested, are already being performed under the Board's interim standard. A number of commenters suggested that the effective date of the new standard be linked to the beginning of an engagement period, rather than to the report issuance date, so that firm personnel could familiarize themselves with the new requirements before beginning work on engagements subject to the new standard.

While the Board is sympathetic to concerns that implementing the new EQR requirements in the middle of an engagement could be disruptive, it also believes that it is important to strengthen the existing requirements as soon as practicable. The Board recognizes that implementing the new standard on EQRs of interim reviews in 2009 may not be possible because some of the interim reviews will be performed earlier in the year, and registered firms would not have sufficient time for implementation of the

^{38/} Paragraphs 12 and 17 of the new proposal.

^{39/} Like the original proposal, the new proposal prohibits the firm from granting the client permission to use the engagement report (or communicating an engagement conclusion if no report is issued) until the reviewer provides concurring approval of issuance.



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new requirements. Therefore, for EQRs of interim reviews, the Board intends to make a final standard effective, subject to approval by the SEC, for fiscal years beginning after December 15, 2009. For EQRs of audits, however, the Board intends to make a final standard effective, subject to SEC approval, for audits of fiscal years ending on or after December 15, 2009.

III. Opportunity for Public Comment

The Board will seek comment for a 45-day period. Interested persons are encouraged to submit their views to the Board. Written comments should be sent to the Office of the Secretary, PCAOB, 1666 K Street, N.W., Washington, D.C. 20006-2803. Comments also may be submitted by e-mail to comments@pcaobus.org or through the Board's Web site at www.pcaobus.org. All comments should refer to PCAOB Rulemaking Docket Matter No. 025 in the subject or reference line and should be received by the Board no later than 5:00 PM (EST) on April 20, 2009.

The Board will consider all comments received. Following the close of the comment period, the Board will determine whether to adopt final rules, with or without amendments. Any final rules adopted will be submitted to the SEC for approval. Pursuant to Section 107 of the Act, proposed rules of the Board do not take effect unless approved by the Commission. Standards are rules of the Board under the Act.

On the 4th day of March, in the year 2009, the foregoing was, in accordance with the bylaws of the Public Company Accounting Oversight Board,

ADOPTED BY THE BOARD.

/s/ J. Gordon Seymour

J. Gordon Seymour
Secretary

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Auditing Standard No. X

Supersedes SECPS Requirements of Membership § 1000.08(f).

Engagement Quality Review

Applicability of Standard

1. An engagement quality review and concurring approval of issuance are required for each audit engagement and for each engagement to review interim financial information conducted pursuant to the standards of the Public Company Accounting Oversight Board ("PCAOB").

Objective

2. The objective of the engagement quality reviewer is to perform an evaluation of the significant judgments made by the engagement team and the conclusions reached in forming the overall conclusion on the engagement and in preparing the engagement report, if a report is to be issued, in order to determine whether to provide concurring approval of issuance.^{1/}

Qualifications of an Engagement Quality Reviewer

3. An engagement quality reviewer may be a partner of the firm that issues the engagement report (or communicates an engagement conclusion, if no report is issued), another individual in an equivalent position in the firm, or an individual outside the firm. The engagement quality reviewer must be an associated person of a registered public accounting firm.

^{1/} In the context of an audit, "engagement report" refers to the audit report (or reports if, in an integrated audit, the auditor issues separate reports on the financial statements and internal control over financial reporting). In the context of an engagement to review interim financial information, the term refers to the report on interim financial information. An engagement report might not be issued in connection with a review of interim financial information. See paragraph .03 of AU section ("sec.") 722, *Interim Financial Information*.



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4. As described below, an engagement quality reviewer must have competence, independence, integrity, and objectivity.

Note: The firm's quality control policies and procedures should include provisions to provide the firm with reasonable assurance that the engagement quality reviewer has sufficient competence, independence, integrity, and objectivity to perform the engagement quality review in accordance with the standards of the PCAOB.

5. *Competence.* The engagement quality reviewer must possess the level of knowledge and competence related to accounting, auditing, and financial reporting required to serve as the person who has overall responsibility for the same type of engagement.^{2/}

6. *Independence, Integrity, and Objectivity.* The engagement quality reviewer must be independent of the company, perform the engagement quality review with integrity, and maintain objectivity in performing the review.

Note: The reviewer may use assistants in performing the engagement quality review. Personnel assisting the engagement quality reviewer also must be independent, perform the assigned procedures with integrity, and maintain objectivity in performing the review.

7. To maintain objectivity, the engagement quality reviewer should not: (a) make decisions on behalf of the engagement team; (b) assume any of the responsibilities of the engagement team; or (c) supervise the engagement team with respect to the engagement subject to the engagement quality review. The person who has overall responsibility for the engagement remains responsible for the engagement and its performance, notwithstanding the involvement of the engagement quality reviewer.

8. The engagement quality reviewer may not be the person who had overall responsibility for either of the two audits preceding the audit subject to the engagement quality review.

^{2/} PCAOB interim quality control standards describe the competencies required of a person who has the overall responsibility for an engagement (or any practitioner-in-charge of an attest engagement). See QC sec. 40, *The Personnel Management Element of a Firm's System of Quality Control-Competencies Required by a Practitioner-in-Charge of an Attest Engagement*.



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Engagement Quality Review for an Audit

9. *Engagement Quality Review Process.* In an audit engagement, the engagement quality reviewer should evaluate the significant judgments made by the engagement team and the conclusions reached in forming the overall conclusion on the engagement and in preparing the engagement report. To identify and evaluate the significant judgments and conclusions, the engagement quality reviewer should perform the procedures described in paragraph 10 by holding discussions with the person with overall responsibility for the engagement, by holding discussions with other members of the engagement team as necessary, and by reviewing documentation.

10. In an audit, the engagement quality reviewer should:

- a. Evaluate engagement planning, including –
 - The consideration of the firm's recent engagement experience with the company and risks identified in connection with the firm's client acceptance and retention process,
 - The consideration of the company's business, recent significant activities, and related financial reporting issues and risks, and
 - The judgments made about materiality and the effect of those judgments on the engagement strategy.
- b. Evaluate the risk assessments and audit responses, including the identification of significant risks, including fraud risks, and the engagement procedures performed in response to significant risks.
- c. Review the engagement team's evaluation of the firm's independence in relation to the engagement.
- d. Evaluate judgments made about (1) the materiality and disposition of corrected and uncorrected identified misstatements and (2) the severity and disposition of identified control deficiencies.
- e. Determine if appropriate matters have been communicated, or identified for communication to the audit committee, management, and other parties, such as regulatory bodies.



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- f. Determine if appropriate consultations have taken place on difficult or contentious matters. Review the documentation, including conclusions, of such consultations.
 - g. Read the financial statements, management's report on internal control, and the related engagement report.
 - h. Read other information in documents containing the financial statements to be filed with the Securities and Exchange Commission ("SEC")^{3/} and evaluate whether the engagement team has taken appropriate action with respect to any material inconsistencies with the financial statements or material misstatements of fact of which the engagement quality reviewer is aware.
 - i. Review the engagement completion document^{4/} and confirm with the person who has overall responsibility for the engagement that there are no significant unresolved matters.
11. *Evaluate Engagement Documentation.* In an audit, the engagement quality reviewer should evaluate whether the engagement documentation that he or she reviewed when performing the procedures required by paragraph 10 –
- a. Indicates that the engagement team responded appropriately to significant risks, and
 - b. Supports the conclusions reached by the engagement team with respect to the matters reviewed.
12. *Concurring Approval of Issuance.* In an audit, the engagement quality reviewer may provide concurring approval of issuance only if, after performing with due

^{3/} See paragraphs .04-.06 of AU sec. 550, *Other Information in Documents Containing Audited Financial Statements*; AU sec. 711, *Filings Under Federal Securities Statutes*.

^{4/} PCAOB Auditing Standard No. 3, *Audit Documentation*, requires the auditor to identify all significant findings or issues in an engagement completion document.



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professional care^{5/} the review required by this standard, he or she is not aware of a significant engagement deficiency.

Note: A *significant engagement deficiency* in an audit exists when (1) the engagement team failed to obtain sufficient appropriate evidence in accordance with the standards of the PCAOB, (2) the engagement team reached an inappropriate overall conclusion on the subject matter of the engagement, (3) the engagement report is not appropriate in the circumstances, or (4) the firm is not independent of its client.

13. In an audit, the firm may grant permission to the client to use the engagement report only after the engagement quality reviewer provides concurring approval of issuance.^{6/}

Engagement Quality Review for a Review of Interim Financial Information

14. *Engagement Quality Review Process.* In an engagement to review interim financial information, the engagement quality reviewer should evaluate the significant judgments made by the engagement team and the conclusions reached in forming the overall conclusion on the engagement and in preparing the engagement report, if a report is to be issued. To identify and evaluate the significant judgments and conclusions, the engagement quality reviewer should perform the procedures described in paragraph 15 by holding discussions with the person with overall responsibility for the engagement, by holding discussions with other members of the engagement team as necessary, and by reviewing documentation.

15. In a review of interim financial information, the engagement quality reviewer should:

- a. Evaluate engagement planning, including the consideration of –

^{5/} See AU sec. 230, *Due Professional Care in the Performance of Work*.

^{6/} Concurring approval of issuance by the engagement quality reviewer also is required when reissuance of an engagement report requires the auditor to update his or her procedures for subsequent events. In that case, the engagement quality reviewer should update the engagement quality review by addressing those matters related to the subsequent events procedures.



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- The firm's recent engagement experience with the company and risks identified in connection with the firm's client acceptance and retention process,
 - The company's business, recent significant activities, and related financial reporting issues and risks, and
 - The nature of identified risks of material misstatement due to fraud.
- b. Perform the procedures described in paragraphs 10.c through 10.f.
 - c. Read the interim financial information for all periods presented and for the immediately preceding interim period, management's disclosure for the period under review, if any, about changes in internal control over financial reporting, and the related engagement report, if a report is to be filed with the SEC.
 - d. Read other information in documents containing interim financial information to be filed with the SEC^{7/} and evaluate whether the engagement team has taken appropriate action with respect to material inconsistencies with the interim financial information or material misstatements of fact of which the engagement quality reviewer is aware.
 - e. Review the engagement completion document and confirm with the person who has overall responsibility for the engagement that there are no significant unresolved matters.

16. *Evaluate Engagement Documentation.* In a review of interim financial information, the engagement quality reviewer should evaluate whether the engagement documentation that he or she reviewed when performing the procedures required by paragraph 15 –

- a. Indicates that the engagement team responded appropriately to significant risks, and
- b. Supports the conclusions reached by the engagement team with respect to the matters reviewed.

^{7/} See paragraph .18f of AU sec. 722, *Interim Financial Information*; AU sec. 711, *Filings Under Federal Securities Statutes*.



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17. *Concurring Approval of Issuance.* In a review of interim financial information, the engagement quality reviewer may provide concurring approval of issuance only if, after performing with due professional care the review required by this standard, he or she is not aware of a significant engagement deficiency.

Note: A *significant engagement deficiency* in a review of interim financial information exists when (1) the engagement team failed to perform interim review procedures necessary in the circumstances of the engagement, (2) the engagement team reached an inappropriate overall conclusion on the subject matter of the engagement, (3) the engagement report is not appropriate in the circumstances, or (4) the firm is not independent of its client.

18. In a review of interim financial information, the firm may grant permission to the client to use the engagement report (or communicate an engagement conclusion to its client, if no report is issued) only after the engagement quality reviewer provides concurring approval of issuance.

Documentation of an Engagement Quality Review

19. Documentation of an engagement quality review should be included in the engagement documentation and should contain sufficient information to identify:

- a. The engagement quality reviewer and others who assisted the reviewer,
- b. The documents reviewed by the engagement quality reviewer and others who assisted the reviewer,
- c. The significant discussions held by the engagement quality reviewer and others who assisted the reviewer, including the date of each discussion, the specific matters discussed, the substance of the discussion, and the participants, and
- d. The date the engagement quality reviewer provided concurring approval of issuance or, if no concurring approval of issuance was provided, the reasons for not providing the approval.

20. The requirements related to retention of and subsequent changes to audit documentation in AS No. 3 apply with respect to the documentation of the engagement quality review.

**Exhibit 2(a)(E)****Alphabetical List of Comments**

BDO Seidman, LLP

California Society of Certified Public Accountants, Mark F. Wille, Chair,
Accounting Principles and Auditing Standards Committee

Center for Audit Quality, Cynthia M. Fornelli, Executive Director

Computer Sciences Corporation, Donald G. DeBuck, Vice President and
Corporate Controller

Crowe Horwath LLP

Deloitte & Touche LLP

Eli Lilly and Company, Arnold C. Hanish, Vice President and Chief Accounting
Officer

Ernst & Young LLP

Financial Executives International, Arnold C. Hanish, Chairman, Committee on
Corporate Reporting

James L. Fuehrmeyer

Grant Thornton LLP

Illinois CPA Society, Jon R. Hoffmeister, Chair, Audit and Assurance Services
Committee

Institut der Wirtschaftspruefer

KPMG LLP

Mantyla McReynolds, LLC, Jon E. Lelegren, Assurance Partner

Mayer Hoffman McCann P.C.
Mazars, Jean-Luc Barlet, Risk Management & Audit Quality
McGladrey & Pullen, LLP
Moss Adams LLP
New York State Society of CPAs
Otter Tail Corporation, Debra Wilke, Director, Corporate Accounting
Piercy, Bowler, Taylor & Kern
PricewaterhouseCoopers LLP
Reznick Group. P.C.
Texas Society of CPAs, Melissa A. Frazier, Chair, Professional Standards Committee
The Institute of Chartered Accountants in England and Wales
United States Chamber of Commerce
United States Government Accountability Office
Xerox Corporation, Gary R. Kabureck, Vice President, Chief Accounting Officer

April 20, 2009

Via e-mail: comments@pcaobus.org

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

Re: PCAOB Release No. 2009-001, Rulemaking Docket Matter No. 025
Proposed Auditing Standard – Engagement Quality Review

Dear Board Members and Staff:

BDO Seidman, LLP appreciates the opportunity to provide comments on the re-proposed auditing standard, *Engagement Quality Review* (the “proposed standard”). We commend the Board for its careful consideration of comments received on the previously proposed standard and its re-proposal in light of the significant revisions made. We support the issuance of enhanced guidance that contributes to an effective engagement quality review (“EQR”) process, as such a process is fundamental to audit quality.

While we support the issuance of this proposed standard, we continue to believe that the best approach to the development of high quality auditing standards is to work with the International Auditing and Assurance Standards Board (“IAASB”) and to converge with the International Standards on Auditing (“ISAs”) when appropriate in the context of the U.S. public company environment. Such an approach would be consistent with convergence efforts of the Auditing Standards Board and other standard setters and ensure the development of a single set of standards for use around the world. We encourage the Board to consider the benefits of convergence in relation to this proposed standard and in the development of all other standards. As we more fully describe in later sections of this comment letter, choosing to select only specific attributes of the ISAs into the proposed standard, such as inclusion of an objective, without the context and authority within which the objective is considered, presents certain complexities in implementing the standard.

Our comments to the questions posed in the Release accompanying the proposed standard (the “Release”) are provided below for your consideration.



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A. Applicability of the EQR Requirement

- 1. Should the standard require an EQR for other kinds of engagements performed according to PCAOB standards? If so, what type of engagements should be included and what should an EQR of such engagements entail?**

We support restricting the applicability of the proposed standard to audits and reviews of interim financial information. While we believe that investors and other users of financial information expect that any engagement performed according to the Board's standards should be subject to a quality control review by an objective and qualified professional outside the engagement team before issuance, the construct of the proposed standard is such that it is tailored to audits and interim reviews and accordingly should apply only to these specific types of engagements. To ensure the proper attention to quality in other types of engagements (e.g., attestation engagements), we recommend the development of separate engagement quality control standards for these types of engagements.

B. Objective of the Standard

- 2. Is the objective in the repropoed standard appropriately formulated? Does it articulate the purpose of an EQR?**

As set out in our comment letter on the original proposed EQR standard, dated May 9, 2008, we support including an explicitly stated overall objective of the engagement quality review in the proposed standard. The inclusion of an objective supports the principles-based audit approach and, as stated in the Release, serves to focus the auditor's attention on the "big picture."

While we support the use of objectives in all auditing standards, we believe that the current formulation may not be as clear as it might be and suggest the following revisions to more clearly focus the objective. (Deletions are shown as strikethrough text and additions in italics.)

The objective of the engagement quality reviewer is to:

- (a) ~~perform an~~ *evaluate* ~~ion~~ of the significant judgments made by the engagement team and the conclusions reached in forming the overall conclusion on the engagement and in preparing the engagement report, if a report is to be issued; ~~and in order to determine~~



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- (b) *assess the appropriateness of providing ~~whether to provide~~ concurring approval of issuance based on such an evaluation, using due professional care.*

3. Will this objective contribute to a more thoughtful and effective EQR?

Objectives provide a framework for the auditor to assess whether or not in his or her judgment the procedures performed were sufficient to satisfy the stated objective, even when all required procedures as set out in the standard were performed. The clear articulation of an objective of an EQR provides the context within which the auditor exercises professional judgment in the performance of review procedures.

However, as stated in the forepart, we believe that to achieve the full benefit of using objectives within this and any other standards promulgated by the PCAOB, the authority of the objective needs to be defined within the context of a broader standard, and we recommend the development of such a standard. The IAASB has accomplished this through the issuance of ISA 200, *Overall Objectives of the Independent Auditor and the Conduct of an Audit in Accordance with International Standards on Auditing*. (See also our response to question 9 below.)

C. Qualifications of the Engagement Quality Reviewer

4. Is it appropriate to explicitly require a reviewer from within the firm to be a partner or an individual in an equivalent position?

We continue to believe that paragraph 5 seems to imply that the engagement quality reviewer's skills are expected to match those of the engagement partner. While the Release indicates that the engagement quality reviewer's skills are not required to identically match those of the engagement partner, this is not clear in the language of the standard. In any event, we suggest that a better approach would be to define the attributes of an engagement quality reviewer, similar to what is done in International Standard on Quality Control 1, *Quality Control for Firms that Perform Audits and Reviews of Financial Statements, and Other Assurance and Related Services Engagements*.

We agree that it is appropriate to explicitly require a reviewer from within the firm to be a partner; however, we are unsure about the meaning of the phrase "or an individual in an equivalent position." While we recognize that this phrase is used in Regulation S-X, its meaning is not sufficiently clear. For instance, does this phrase mean that a director (a non-partner position) in a firm that is organized as a



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partnership would qualify as a reviewer? The discussion at the open Board meeting held on March 4, 2009, to consider reproposing this EQR standard, seemed to suggest that the phrase “or an individual in an equivalent position” only pertained in the circumstance where the firm structure was not a partnership. If this is the intention, we suggest providing a footnote to the phrase “the engagement quality reviewer would be another individual in an equivalent position in the firm” that clarifies that this situation would arise only in situations where the firm structure is not a partnership.

5. Should the standard allow qualified accountants who are not employed by an accounting firm to conduct the review?

As set out in the proposed standard, we believe that it is appropriate to allow qualified accountants who are not employed by an accounting firm to conduct an EQR. This provision is consistent with the existing interim standards and is necessary to accommodate smaller and medium-sized firms where there may not be other partners with sufficient experience in a particular industry or who meet the independence or objectivity criteria to conduct the review. As the proposed standard is principles-based, the general competence requirement as set out in paragraph 5 of the proposed standard, amended as provided in our response to question 4 above, would provide the basis for selection of an appropriate engagement quality reviewer from outside the firm.¹ The general competence requirement in the proposed standard provides a sufficiently high competency standard while providing flexibility in the selection of appropriate reviewers.

6. Should the standard prohibit the engagement partner from serving as the reviewer for a period of time following his or her last year as the engagement partner? If so, is two years sufficient, or should it be extended?

We agree that the standard should prohibit the engagement partner from serving as the reviewer for a period of time following his or her last year as the engagement partner to ensure the appropriate level of objectivity in the review process. While recognizing that the experience gained as an engagement partner on a specific engagement provides a unique perspective a reviewer can draw upon, we believe that a two year period following serving as the engagement partner is a reasonable time period for promoting objectivity.

¹ Paragraph 5 of the proposed standard states, “The engagement quality reviewer must possess the level of knowledge and competence related to accounting, auditing, and financial reporting required to serve as the person who has overall responsibility for the same type of engagement.”



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D. EQR Process

- 7. Are the descriptions of the scope and extent of EQR procedures contained in the repropoed standard appropriate? Will the performance of these procedures result in a high-quality EQR? If not, how should these procedures be revised?**

We agree that the scope and extent of EQR procedures described in the proposed standard are appropriately focused on the significant judgments made by the engagement team and the conclusions reached in forming the overall conclusion on the engagement. As currently drafted, we recognize that the reviewer is not expected to obtain “independent evidence” or perform procedures that duplicate those performed by the engagement team in order to evaluate the significant judgments and conclusions made by the engagement team, but rather is expected to identify and evaluate these matters through discussion with the engagement partner and team members as necessary and by reviewing documentation; we support such an approach.

However, as noted in our comment letter on the previously proposed EQR standard dated May 9, 2008, we believe that additional guidance is necessary with respect to a mechanism for the resolution of disagreements between the engagement partner and the engagement quality reviewer. We believe that this guidance should require any conclusions reached to be documented in accordance with the provisions of AS No. 3, paragraph 8, and that the report should not be issued until the matter is resolved in accordance with a firm established framework for the resolution of such differences.

We also believe that that the standard should encourage timely involvement of the engagement quality reviewer as the engagement progresses. This would tend to promote identification and resolution of significant issues early in the engagement.

- 8. Are the specifically required procedures appropriately tailored to reflect the difference in scope between an audit and an interim review?**

We agree that the specifically tailored procedures set out in the proposed standard are appropriately tailored to reflect the difference in scope between an audit and an interim review.



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9. Do the specifically required procedures sufficiently focus the reviewer on areas of highest risk? Are there other procedures that should be required?

We believe that the procedures specifically required in paragraph 10 for an audit and paragraph 15 for a review of interim financial information appropriately focus the reviewer on the areas of highest risk and that other procedures are not required to meet the objective of the EQR. While the specific procedures described in the standard are required in all circumstances, the use of the objective within the standard provides the “big-picture” perspective whereby the reviewer would assess whether additional procedures were necessary to meet that objective. While we believe that this perspective is necessary, we do not believe that the current structure of the PCAOB standards supports the functioning of the objective such that it provides for the performance of additional procedures when such procedures are necessary to achieve the objective. To realize the full benefit of including an objective within the standard we believe that an ISA 200-like standard is necessary and should be developed.

E. Concurring Approval of Issuance

10. Is the standard for the engagement quality reviewer’s concurring approval of issuance appropriately described in the repropoed standard? Is the first condition appropriately tailored to reflect the difference in scope between an audit and an interim review?

We agree that the due professional care standard is the correct standard to use in the context of determining whether a reviewer has a sufficient basis to make a meaningful decision about whether to provide concurring approval of issuance. The use of the phrase “knows or should know based upon the requirements of the standard” in the previously proposed standard was sufficiently vague in that it created the potential for second guessing about what a reviewer should have known before providing concurring approval of issuance. However, since the Release itself essentially equates “due professional care” with a “knows or should have known...” criterion, our previously expressed concerns have not been addressed satisfactorily.

In addition, the first item included within the note to paragraph 12 relating to an audit and paragraph 17 relating to a review, regarding the existence of significant deficiencies, are appropriately tailored.



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F. Documentation of the EQR

**11. Are the documentation requirements in the repropoed standard appropriate?
If not, how should they be changed?**

We agree that generally the documentation requirements presented in the proposed standard have appropriately replaced the somewhat broad documentation requirements of the previous proposal, such that there is more specificity about what needs to be documented in order to ensure that both the Board, as part of their inspection responsibility, and firms are able to understand how an EQR was conducted and how significant issues were resolved by the engagement team through review of documentation. However, we believe the requirement in paragraph 19(c) to document discussions between the engagement quality reviewer and the engagement team is not necessary and would not be cost-effective. The engagement quality reviewer ordinarily has numerous discussions with members of the engagement team during the course of an audit. It is not always practical to document such discussions on a timely basis. Moreover, the issues discussed already should be documented in the workpapers subject to his or her review and the requirement in paragraph 19(b) would document the engagement quality reviewer's review of those workpapers. Therefore, the additional documentation called for by 19(c) would be redundant.

We appreciate your consideration of our comments and suggestions, and would be pleased to discuss these with you at your convenience. Please direct any questions to Wayne Kolins, National Director of Assurance at 212-885-8595 (wkolins@bdo.com) or Susan Lister, National Director of Audit Policy at 212-885-8375 (slister@bdo.com).

Very truly yours,

/s/ BDO Seidman, LLP

BDO Seidman, LLP

April 15, 2009



California
Society

Certified
Public
Accountants

Office of the Secretary
Public Company Accounting Oversight Board
1666 K Street, N.W.
Washington, D.C.
20006-2803

Re: Response to PCAOB Rule-Making Docket Matter No. 025

Transmitted by email to: comments@pcaobus.org

To the Members of the PCAOB:

The Accounting Principles and Auditing Standards Committee (the AP&AS “Committee”) of the California Society of Certified Public Accountants (CALCPA) is pleased to provide our comments to the Public Company Accounting Oversight Board (PCOAB) on PCAOB Rule Making Docket Matter No. 025, “Proposed Auditing Standard Engagement Quality Review.”

The AP&AS Committee is the senior technical committee of CALCPA. CALCPA has approximately 32,000 members. The Committee is comprised of 50 members, of whom 67 percent are from local or regional firms, 23 percent are sole practitioners in public practice, 5 percent are in industry and 5 percent are in academia.

The Committee has submitted its response in the following order: First, the Committee has provided its response to the PCAOB’s questions set forth on pages 8-26 of the Release. Second, the Committee has provided certain other observations for the PCAOB’s consideration.

We thank you for the opportunity to comment on this matter. We would be glad to discuss our opinions further, should the PCAOB have any questions or require any additional information.

Very truly yours,

A handwritten signature in black ink, appearing to read 'M. Wille', with a long horizontal flourish extending to the right.

Mark F. Wille, Chair
Accounting Principles and Auditing Standards Committee
California Society of Certified Public Accountants

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COMMENTS REGARDING THE PCAOB'S
REVISED PROPOSED AUDITING STANDARD
ENGAGEMENT QUALITY REVIEW

The Committee supports the overall direction of the repropoed Standard, as the PCAOB was responsive to the strong sentiments expressed in the comment letters received last year. It is clear the term "robust review" included on page 3 of the Release was implemented in the detail procedures set forth in the Standard.

Question 1: Should the Standard require an EQR for other kinds of engagements performed according to PCAOB standards? If so, what types of engagements should be included and what should an EQR of such engagements entail?

Response: The PCAOB identified two primary types of engagements excluded from the scope of the Standard: (1) engagements performed pursuant to Auditing Standard No. 4, Reporting on Whether a Previously Reported Material Weakness Continues to Exist, and (2) engagements required by the SEC's Regulation AB. The Committee believes that audit firms who perform attestation engagements under Regulation AB routinely include such engagements under their firm's quality review program. Accordingly, the Committee supports expanding EQR standards to engagements other than audits and interim reviews. However, the Committee suggests the PCAOB address this issue in a separate standard to facilitate timely release of the current repropoed Standard.

Question 2: Is the objective in the repropoed standard appropriately formulated? Does it articulate the purpose of the EQR?

Response: The Committee believes that the Standard is best stated in terms of the clear objectives of the EQR process and the qualifications of the reviewer. The reviewer should then work to achieve the objectives of the EQR. The Committee believes that to mix the objectives of the EQR with the objectives of the reviewer in achieving them is not useful, and could lead to a reviewer narrowing the scope of the EQR to meet the stated objectives of the reviewer rather than broader objectives of the EQR. Further, the Committee does not believe the emphasis of the responsibilities of the reviewer that the Board is seeking by phrasing the objectives of the EQR as objectives for the reviewer is necessary; a qualified reviewer will clearly understand those responsibilities.

Question 3: Will this objective contribute to a more thoughtful and effective EQR?

Response: The Committee believes the repropoed Standard will provide clarity to the EQR process within audit firms, thus providing a more thoughtful and effective EQR.

Question 4: Is it appropriate to explicitly require a reviewer from within the firm to be a partner or an individual in an equivalent position?

Response: The Committee believes the person ultimately responsible for the quality review can delegate portions of the review to a non-partner in the firm, working under the supervision of the assigned quality reviewer. The level of knowledge required for a quality reviewer might, in part, be held by other persons participating in the review under the supervision of the quality reviewer. The engagement partner can rely on others for knowledge, and the quality reviewer should similarly be able to rely on others for knowledge.

Question 5: Should the standard allow qualified accountants who are not employed by an accounting firm to conduct the review?

Response: Use of outside, qualified, personnel may be critical if smaller registered accounting firms are to continue to perform PCAOB audits. In that regard, the Committee recommends the PCAOB clarify the term “associated person” with regard to how a registered accounting firm might utilize the contract services of an individual outside the registered accounting firm, as set forth in paragraph 3 of the Standard. The second sentence of paragraph 3, of the proposed Standard uses the phrase “associated person of a registered public accounting firm.” The Committee recommends that the Board add, by way of a footnote, the definition of “associated person” or a cross-reference to where it is defined. It would also be helpful to use the phrase “person associated with a registered public accounting firm” which is the term used in Form I.

Question 6: Should the standard prohibit the engagement partner from serving as the reviewer for a period of time following his or her last year as the engagement partner? If so, is two years sufficient, or should it be extended?

Response: The Committee disagrees with the PCAOB’s adoption of a two year hiatus between functions when the engagement partner has served less than five years in that function. The existing partner rotation standard of five years on and five years off the engagement ought to be applied, irrespective of whether the individual served in the capacity of engagement partner or concurring reviewer during the maximum permitted five year relationship period. Including this additional, two year period as a requirement will unduly impact the smaller registered accounting firm’s ability to assign qualified partner-level personnel to the engagement. The Committee is not aware of any empirical evidence to suggest that prior service as an engagement partner will taint the objectivity of that person performing the quality review in the following year.

Question 7: Are the descriptions of the scope and extent of EQR procedures contained in the repropoed standard appropriate? Will the performance of these procedures result in a high-quality EQR? If not, how should these procedures be revised?

Response: The Committee supports the separation between EQR procedures applicable to the audit and interim review processes. The descriptions, scope and extent of EQR procedures are adequately described. However, a relatively minor revision is suggested as follows: Substitute the term “firm’s client” for the term “company” beginning in paragraph 10. a. on page A1-3 of the Standard, and make such change consistent throughout the remainder of the document. The Committee believes that “firm’s client” is a more precise reference to the entity under audit or review than the term “company.”

Question 8: Are the specifically required procedures appropriately tailored to reflect the difference in scope between an audit and an interim review?

Response: The Committee agrees that the procedures are reasonably tailored between an audit and interim review. However, we would suggest specifically listing the procedures referred to in paragraph 15 b. on page A1-6 of the Standard, instead of referring the reader to the “procedures described in paragraphs 10.c through 10. f,” which are applicable to an audit. For example, step 10.d. (2) on page A1-3 of the Standard requires the engagement reviewer to: “Evaluate judgments made about the severity and disposition of identified control deficiencies.” We recommend this required procedure be redrafted to specifically apply to the more limited inquiries related to internal controls conducted in a review of interim information. The auditor’s inquiries regarding internal controls during a review of interim financial information are generally limited to inquiries of management regarding identifying changes in internal controls, or the remediation or previously identified control deficiencies. Testing the effectiveness of internal controls based on management’s assertions or identifying new control deficiencies are processes generally reserved for the integrated audit performed at the end of the fiscal year.

Question 9: Do the specifically required procedures sufficiently focus the reviewer on areas of highest risk? Are there other procedures that should be required?

Response: The procedures as proposed provide sufficient flexibility under the stated objective of the EQR process to enable the reviewer to focus attention on areas of “significant judgments” reached by the engagement team. However, we have several specific observations:

Paragraph 10.h. would require the reviewer to read other information in documents containing financial statements to be filed with the Securities and Exchange Commission, with a footnote 3 reference to AU 550.04-.06 and AU 711. As written, this procedure imposes a task on the reviewer for filings under the Securities Act of 1933 that is beyond the requirements of existing auditing literature. It also imposes an unrealistic and unnecessary burden on the reviewer. This information is often voluminous, especially if one considers exhibits typically included or incorporated into SEC filings, and certain information in the body of a document may not be relevant or necessary to the EQR. The Committee strongly recommends that the procedure be changed from “read” to “consider.”

AU 550.02 and .03 in defining the scope of “other information” specifically exclude other information included in filings under the Securities Act of 1933. The Committee recommends that footnote 3 be revised to include reference to AU 550.02 and .03 and that it be clarified that AU 550 and AU 711 specify the auditor’s responsibility to consider other information. The

Committee suggests: “See paragraphs .01-.06 of AU sec. 550, Other Information in Documents Containing Audited Financial Statements; AU sec. 711, Filings Under Federal Securities Statutes for the auditor’s responsibility to consider other information.”

Question 10: Is the standard for the engagement quality reviewer's concurring approval of issuance appropriately described in the repropoed standard? Is the first condition appropriately tailored to reflect the difference in scope between an audit and an interim review?

Response: The Committee believes the language of the repropoed Standard's focus on "due professional care" is an appropriate benchmark. However, the Committee is troubled by the PCAOB's inclusion of its view that: "While auditors should be more familiar with "due professional care" than the concurring approval standard in the original proposal, the requirement to exercise due professional care imposes on a reviewer essentially the same requirement as the "knows, or should know based on the requirements of this standard" formulation in the board's original proposal (emphasis added)." This language, which was included on page 24 of the Release, will create practical confusion in the implementation of the repropoed Standard. This editorial amplification should be removed from the final standard.

The Committee supports the inclusion, in the same paragraph on page 24, of the following sentence: "At the same time, eliminating the phrase "should know" from the repropoed standard should alleviate commenters' concerns that the Board would evaluate decisions to provide concurring approval of issuance with the benefit of hindsight."

Question 11: Are the documentation requirements in the reported standard appropriate? If not, how should they be changed?

Response: The Committee agrees that the matters requiring documentation set forth in paragraph 19 on page A1-7 of the Standard are important to rectify certain apparent voids noted during the PCAOB's inspection of engagements. However, some examples of the means by which such documentation may be evidenced would help registered audit firms comply with the Standard. For example, the majority of registered audit firms utilize some form of paperless audit documentation. Accordingly, it is a common practice for the designated quality reviewer to evidence review of specific work papers by electronically "signing off" the binder index line item corresponding to the specific work paper. The Committee believes that such a sign off would constitute acceptable evidence of completing step 19. b. on page A-7 of the Standard. Therefore, The Committee suggests a statement be added to paragraph 19. permitting flexibility in the manner of documenting the required items.

Other Comments:

Effective Date: The Committee recommends that the effective date of the proposed EQR standard for audits be no sooner than years beginning thirty days after the issuance of a final EQR standard. As proposed, the EQR standard would be effective for audits for fiscal years ending on or after December 15, 2009. Audit planning and procedures for many audit engagements for fiscal years ending on or after December 15, 2009 will be well underway by the time a final EQR standard is issued. To have the EQR standard effective for audits commenced before issuance of the EQR standard may be unduly burdensome, especially in situations where the concurring partner currently assigned does not meet the new criteria of the new EQR standard.



EXECUTIVE DIRECTOR

Cynthia M. Fornelli

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April 20, 2009

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

Re: Request for Public Comment: *Proposed Auditing Standard – Engagement Quality Review, PCAOB Rulemaking Docket Matter No. 025*

Dear Office of the Secretary:

The Center for Audit Quality (CAQ or the Center) is a public policy organization that seeks to foster confidence in the audit process and to aid investors and the capital markets by advancing constructive suggestions for reform that are rooted in the profession's core values of integrity, objectivity, honesty, and trust. We also seek to improve the reliability of public company audits and to enhance their relevance for investors in this time of increasing globalization and financial complexity. Any U.S. accounting firm registered with the Public Company Accounting Oversight Board (PCAOB or the Board) may join the CAQ. The CAQ is affiliated with the American Institute of Certified Public Accountants (AICPA) and has approximately 750 U.S. public company audit firms as members, representing tens of thousands of professionals dedicated to audit quality.

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We welcome the opportunity to share our views¹ on the PCAOB's Proposed Auditing Standard – *Engagement Quality Review (EQR)* (the revised proposal).

We strongly support auditing standards that promote audit quality and believe that a robust and effective engagement quality review that focuses on significant judgments made and the related conclusions reached by the engagement team furthers that purpose. We commend the PCAOB for considering feedback from constituents on its original proposal and for exposing a revised proposal. We believe that compared to the original proposal, the revised proposal more appropriately defines the requirements of the EQR. However, we believe that additional modifications should be made to the revised proposal in order to, improve its quality, lead to its effective and efficient implementation, and enhance its application in practice.

We have organized our observations and concerns about the revised proposal around the following topics:

- Applicability of the Standard
- Overall Objective
- Qualifications of Engagement Quality Reviewer
- Engagement Quality Review Process for an Audit
- Due Professional Care
- Documentation of an Engagement Quality Review
- Effective Date
- Other Comments
 - Review of Interim Financial Information
 - Relationship of Firm Quality Control

Applicability of the Standard

We support the applicability of the revised proposal, which is limited to audits and reviews of interim financial information and which excludes other engagements such as those performed under the attestation standards. The revised applicability avoids the potential confusion of having requirements related to attestation engagements residing in the auditing standards.

Additionally, we believe the Board's inclusion, in paragraph 15, of those requirements that apply specifically to reviews of interim financial information is very helpful.

¹ This letter represents the views of the CAQ, but not necessarily the views of any specific firm, individual or CAQ Governing Board member.

Overall Objective

We believe that the stated objective for an engagement quality review will guide reviewers in satisfying themselves that, in doing their work, they understood and accomplished the requirements of the standard. Furthermore, by putting the review in the proper perspective, the Board improves the likelihood that third parties -- including other regulators and the public -- will have a consistent understanding of the intent of the standard. Finally, we believe that having an objective is beneficial to providing the appropriate framework for the standard-setting process itself, including laying the groundwork for convergence with the International Standards on Auditing (ISAs), which we support as a long-term goal of the PCAOB.

While we strongly support the inclusion of an objective, we note that the requirement is to perform an evaluation of the “significant judgments made by the engagement team and the conclusions reached.” We suggest a clarification to the objective by stating that the review relates to the “significant judgments made by the engagement team, and the **related** conclusions reached.” We believe that this minor change will make clear that the conclusions that should be the focus of the EQR are those that result from the significant judgments.

Qualifications of Engagement Quality Reviewer

Competence

We agree with the Board that the engagement quality reviewer competency requirement should be “principles-based” and that a general competence standard setting a minimum requirement for the engagement quality reviewer is appropriate.² However, we do not believe the language in paragraph 5 of the revised proposal achieves the Board’s intent to establish a “principles-based” requirement. As written, we are concerned that paragraph 5 may have the unintended consequence of prohibiting qualified persons from performing EQRs and may cause resource constraints, particularly for smaller audit firms.

Specifically, paragraph 5 does not make it clear that the reviewer’s competence is not required to match that of the engagement partner, and the paragraph may not provide sufficient flexibility in assigning an appropriate engagement quality reviewer. Instead language such as “required to serve,” and the reference to “the person who has overall responsibility for the same type of engagement,” will cause inevitable comparisons of the attributes of the engagement quality reviewer to those of the actual engagement partner. We do not believe such comparisons are necessary in assessing the competence of the engagement quality reviewer or that such a comparison is the intention of the Board.³ In

² See Release at page 11.

³ See Release at page 11.

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our experience, it is not always essential for the engagement quality reviewer to have had experience with other companies in the respective industry. Many judgments are made in the assignment of an engagement quality reviewer, including but not limited to, consideration of the qualifications, experience, and knowledge of both the engagement partner and the potential engagement quality reviewer. We also do not believe the Board intended to preclude such judgments in assigning engagement quality reviewers; however, this is not clear in paragraph 5 of the revised proposal.

In addition, as indicated in the note to paragraph 6, the reviewer may use assistants in performing the EQR. Therefore, we believe that the standard should make clear that the competence requirements contemplate the combined skills of the engagement quality reviewer and any assistants.

In order to provide appropriate flexibility in assigning qualified engagement quality reviewers and to make the standard consistent with the Board's stated intentions to provide a principles-based standard setting a minimum requirement, we suggest paragraph 5 be revised as follows:

The engagement quality reviewer must possess, or obtain through utilizing assistants, the level of knowledge and competence related to accounting, auditing, and financial reporting required to perform the role. ~~serve as the person who has overall responsibility for the same type of engagement.~~ The appropriate level of knowledge and competence depends on the circumstances of the engagement including the size and complexity of the engagement.

To make it clear that the PCAOB is setting a “minimum requirement for those who would perform the EQR” and not requiring the engagement quality reviewer to “possess skills identical to those of the engagement partner,”⁴ we recommend changing the paragraph to refer to competencies required to fulfill the role of the engagement quality reviewer rather than the role of the engagement partner. This change is consistent with International Standards on Quality Control (ISQC) 1 (R) paragraph 39. Further, adding the second sentence makes it clear that the assignment of an appropriate engagement quality reviewer involves making judgments based on the facts and circumstances of the engagement, and is consistent with footnote 18 of the Board's initial proposal and ISQC 1(R) paragraph A47. These changes would provide audit firms with sufficient discretion to appropriately identify a qualified engagement quality reviewer.

Objectivity

We support the changes made to the standard to clarify the requirement for the engagement quality reviewer to remain objective. Specifically, we believe that the removal of the note to paragraph 6 of the Board's original proposal (now paragraph 7 of the revised proposal) eliminates the perception that the standard would limit consultation

⁴ See Release at page 11.

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between the engagement team and the engagement quality reviewer. We believe that consultation is an important element of audit quality, and that these changes encourage appropriate consultation without compromising the objectivity of the engagement quality reviewer.

Additionally, we agree with the Board's intention stated in its Release that partners with leadership responsibilities in a firm, region, service, or industry practice should not be precluded from acting as an engagement quality reviewer, however, this intention is not made clear in the language in paragraph 7 of the revised proposal.⁵ While we believe that the changes in paragraph 7 appropriately define "objectivity" in terms of the engagement, and not in terms of the engagement team, we remain concerned that the language does not clearly express the intention of the Board. We recommend adding a footnote to paragraph 7 to articulate the view in the Board's Release, such as "Partners with leadership responsibilities are not precluded from acting as an engagement quality reviewer based upon those responsibilities."

Engagement Quality Review Process for an Audit

Paragraphs 9 and 10 prescribe general and specific requirements for conducting the EQR of an audit. We generally agree with the types of procedures to be performed. However, we recommend certain changes in the text of paragraphs 9 and 10 to reflect the intentions of the Board as set out in the Release and the objective of the standard.

We acknowledge and agree with changes in the revised proposal intended to clarify the extent of documentation that the engagement quality reviewer should review. However, we do not believe the language in paragraph 9 is sufficiently clear to communicate that engagement quality reviewers are able to complete the review by reviewing selected documentation. We note that Paragraph 11 refers to "engagement documentation ...reviewed when performing the procedures required by paragraph 10." However, this same clarification is not articulated in paragraph 9. Accordingly, based on these concerns and others articulated in this letter, we recommend that paragraph 9 be modified as follows:

In an audit engagement, the engagement quality reviewer should evaluate the significant judgments made by the engagement team and the **related** conclusions reached in forming the overall conclusion on the engagement and in preparing the engagement report. To identify and evaluate the significant judgments and **related** conclusions, the engagement quality reviewer should perform the procedures described in paragraph 10 by holding discussions with the person with overall responsibility for the engagement, by holding discussions with other members of the engagement team as necessary, and by reviewing **selected** documentation **as considered necessary by the engagement quality reviewer.**

⁵ See Release at page 14.

The above changes are consistent with: 1) the articulated intention of the revised proposal,⁶ 2) paragraph 11 of the revised proposal, and 3) ISQC 1 (R) paragraph 37.

Further, we believe that the procedures set forth in paragraphs 10.e. and 10.f., which require the reviewer to “determine if appropriate matters have been communicated, or identified for communication” and “determine if appropriate consultations have taken place on difficult or contentious matters” could be interpreted to go beyond the other requirements of the standard that are focused on the evaluation of the work performed by the engagement team. We believe that the procedures in paragraphs 10.e. and 10.f. of the revised proposal should be modified to indicate that the engagement quality reviewer should make an evaluation of the appropriateness of such matters based upon performing all of the other procedures set forth in this standard.

We suggest that these two paragraphs be modified as follows:

e. ~~Determine if~~ *Evaluate whether* appropriate matters *that are identified through the performance of the other engagement quality review procedures in this standard* have been communicated, or identified for communication to the audit committee, management, and other parties, such as regulatory bodies.

f. ~~Determine if~~ *Evaluate whether* appropriate consultations have taken place on difficult or contentious matters *that are identified through the performance of the other engagement quality review procedures in this standard*. Review the documentation, including conclusions, of such consultations.

Alternatively, the Board could include these two procedures in a new paragraph which would follow paragraph 10 and clarify that the evaluation should be made based upon the results of all other procedures performed in accordance with this standard.

Finally, we suggest that the Board modify paragraphs 10.a., 10.b. and 10.d. to make clear that these procedures are intended to apply to significant judgments made by the engagement team. This change is consistent with the direction provided in paragraph 9 and will add appropriate clarity to the requirements.

Due Professional Care

The revised proposal indicates that the engagement quality reviewer “may provide concurring approval of issuance only if, after performing with due professional care the review required by this standard, he or she is not aware of a significant engagement

⁶ During the Board’s open meeting on March 4, 2009 to discuss the revised proposal, Board Member Goelzer asked a question regarding documentation requirements and during that exchange PCAOB staff stated that the engagement quality reviewer is expected to review “selected documentation.”

deficiency.” We agree with and support the description of the basis of conclusions, which is consistent with the Board’s interim standard and the overall objective of an EQR. The revised proposal also requires that the EQR be conducted with due professional care, which we believe is preferable to the “knows or should know” standard of the original proposal.

However, we respectfully disagree with the Board’s suggestion in the Release that “the requirement to exercise due professional care imposes on a reviewer essentially the same requirement as the ‘knows, or should know based on the requirements of this standard’ formulation in the Board’s original proposal.”⁷ Additionally, as explained in our comment letter on the original proposal, we remain concerned that “know or should know” imposes additional responsibilities on a reviewing partner beyond those implied by a “due professional care standard.”

Potts v. SEC, 151 F.3d 810 (8th Cir. 1998), which the Board cites, discusses a standard that resembles the “due professional care” standard proposed by the Board (“Having taken on the concurring review task, Potts also shouldered the duty to perform that task professionally”⁸). However, nothing in that decision suggests that due professional care includes engaging in procedures to ensure that there is nothing the reviewing partner “should have known.” Indeed, the SEC’s and the appellate court’s decisions were based on findings that “[Potts] had acted with *reckless disregard* of his duties as an independent auditor.”⁹ (Emphasis added). His conduct amounted to “an egregious refusal to see the obvious, or to investigate the doubtful.”¹⁰ Because its holding was predicated on recklessness, the court had no occasion to consider whether a concurring partner could be liable where he or she “should have known” (but did not “recklessly disregard”) matters that would have caused him or her to withhold concurring approval.

In light of these considerations, we believe that it is inappropriate for the Board to read into the due professional care standard an element that is not established by precedent and would continue to raise concerns among engagement quality reviewers about the Board’s intent for their performance obligations.

Documentation of an Engagement Quality Review

Paragraph 19(c) requires that the engagement documentation include the significant discussions held by the engagement quality reviewer and others who assisted the reviewer, including the date of each discussion, the specific matters discussed, the substance of the discussion, and the participants. We believe the requirement is

⁷ See Release at Page 24.

⁸ See Potts v. SEC, 151 F.3d 810 (8th Cir. 1998) at 813.

⁹ See Id. at 812

¹⁰ See Id.

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unnecessarily burdensome¹¹, which will result in additional costs that are not likely to provide a commensurate benefit to audit quality. As a result, we recommend it be deleted.

The engagement team's existing obligation to prepare documentation consistent with the objective and requirements of PCAOB Auditing Standard No. 3 *Audit Documentation*, when combined with the revised proposal's requirement to indicate which documents were reviewed by the engagement quality reviewer and his or her assistants, should provide adequate documentation of the basis for the engagement quality reviewer's compliance with the standard.

If the Board continues to believe that it is necessary to document discussions involving the engagement quality reviewer, we recommend that paragraph 19 be revised to include the explanation of what constitutes a "significant discussion" as described in footnote 36 of the Release.

Effective Date

As proposed, the standard would be effective for audits of fiscal years ending on or after December 15, 2009, and for interim reviews for fiscal years beginning after December 15, 2009.

As it relates to audits, we believe that the effective date should be linked to the beginning of an audit engagement period. By linking the effective date to the beginning, the new requirements would: (1) be known and anticipated as of the beginning of the audit engagement period by auditors, audit committees and companies, (2) allow the assigned engagement quality reviewer to comply with the requirements throughout audit engagement planning and execution, and (3) apply equally to each interim review during an audit period to which the revised proposal applies.

Due to the anticipated timing of final approval of the standard by the SEC, we are also concerned that the proposed effective dates would not permit sufficient time for registered public accounting firms to effectively and efficiently implement the new EQR requirements. As proposed, we believe implementation might require significant changes to a firm's quality control processes, particularly those firms that have not historically performed concurring reviews. The effective date should provide all registered public accounting firms with sufficient time to: (1) adopt policies and procedures consistent with the new standard, (2) train their personnel in the requirements of the new standard,

¹¹ For example, an engagement quality reviewer ordinarily has frequent dialog with the engagement team during the course of an engagement. At the time of each discussion, it is unreasonable to expect the engagement quality reviewer to know whether documentation of such discussions ultimately will be necessary to demonstrate compliance with the EQR standard as contemplated in footnote 36 of the Release.

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and (3) assign or engage qualified engagement quality reviewers consistent with their system of quality control.

Accordingly, we believe the PCAOB should base the effective date on fiscal years beginning after December 15, 2009, if the SEC approves the final standard by September 2009, to provide adequate time for firms to prepare for adoption.

Other Comments

Review of Interim Financial Information

As proposed, in a review of interim financial information, the engagement quality reviewer must read the engagement report only if it is filed with the SEC. The final standard should require the engagement quality reviewer to read such a report if issued. Also, given that engagement reports are not issued in every review of interim financial information, the final standard should refer to the engagement quality reviewer's "concurring approval," rather than "concurring approval of issuance."

Relationship to Firm Quality Control

The note to paragraph 4 in the revised proposal contains a presumptively mandatory requirement related to the firm's quality control policies and procedures which, in most cases, is likely to be beyond the control of the engagement quality reviewer or the engagement partner.

The International Auditing and Assurance Board (IAASB) structured its standards according to whom the requirements apply. The ISQCs prescribe requirements for the firm to establish policies and procedures that, among other things, include EQRs. The ISQCs also establish standards on the conduct of the engagement quality reviews, including many requirements similar to those in the revised proposal. The ISAs establish standards for the auditor in the conduct of the audit engagement. We believe that the discipline of keeping the audit firm's requirements in the quality control standards, and the auditor's requirements in the auditing standards and the attestation standards, as appropriate, lends clarity to the requirements in the standards.

* * * *

We appreciate the opportunity to comment on the revised proposal and would welcome the opportunity to respond to any questions you may have regarding any of our comments and recommendations.

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Public Company Accounting Oversight Board
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Sincerely,

A handwritten signature in black ink that reads "Cynthia M. Fornelli". The signature is written in a cursive, flowing style.

Cynthia M. Fornelli
Executive Director
Center for Audit Quality

cc: PCAOB

Mark W. Olson, Chairman
Daniel L. Goelzer, Member
Willis D. Gradison, Member
Steven B. Harris, Member
Charles D. Niemeier, Member
Martin F. Baumann, Chief Auditor and Director of Professional Standards

SEC

Chairman Mary L. Schapiro
Commissioner Luis A. Aguilar
Commissioner Kathleen L. Casey
Commissioner Troy A. Paredes
Commissioner Elisse B. Walter
James L. Kroeker, Acting Chief Accountant
Shelley E. Parratt, Acting Director of the Division of Corporation Finance

Donald G. DeBuck
Vice President and Corporate Controller

April 20, 2009

Office of the Secretary
Public Company Accounting Oversight Board
1666 K Street, N.W., 9TH Floor
Washington, DC 20006-2803

Re: PCAOB Rulemaking Docket Matter No. 25, “Proposed Auditing Standard – Engagement Quality Review”



FILED ELECTRONICALLY (comments@pcaobus.org)

Dear Board Members and Staff,

Thank you for the opportunity to comment on the Public Company Accounting Oversight Board’s (the “Board”) proposed rule, “Proposed Auditing Standard – Engagement Quality Review” Release No. 2009-001 (the “Proposed Standard”), which was issued March 4, 2009. We commend the Board on the changes pursuant to concerns raised in our letter and those of other respondents.

We have supported the efforts of the President, Congress and the Securities and Exchange Commission to enhance investor confidence in the integrity of our financial reporting system. Accurate and reliable financial information is fundamental to investor confidence, and quality audits are an essential component of the US financial reporting system. As a result, auditing standards which address audit quality are critical to high standards for audits of public companies and sustaining the improvements to the financial reporting system in the United States realized through the regulatory refinements enacted under Sarbanes-Oxley.

As previously mentioned, while the Proposed Standard will likely improve audit quality, it is only one of several ways through which audit quality is achieved and we continue to feel it is important to maintain the proper balance between the cost of these measures and resulting benefits. Despite the improvements the current proposal, we remain concerned the Proposed Standard could result in significant costs, disproportionate to the resulting benefits. Accordingly, we think the Board should continue to use every possible means to mitigate the cost of these measures to registrants and, ultimately, investors.

- We continue to have significant concerns regarding the scope of required procedures which must be performed by the engagement quality reviewer and the prohibitively high cost of these audit procedures without commensurate benefits.

- We also believe the scope of procedures and documentation required under the Proposed Standard could significantly impact the timing of the final stages of an audit which could adversely impact the timeliness of issuer filings.

We have provided further information regarding these concerns, as well as other significant comments, concerns and suggestions, in the following paragraphs. We also have included detailed responses in Exhibit I to the specific questions for which the Board is seeking comment.

Scope of Required Procedures

Procedures required under the Proposed Standard are far more exhaustive than practicable or necessary to achieve the necessary assurance. Review of all high risk areas of the engagement for a global client would not only be duplicative but would likely not be feasible. A scope this exhaustive could potentially require a parallel global engagement team working directly under the supervision of the quality reviewer. This would not only result in substantial additional cost without commensurate benefit but could also significantly and adversely impact audit timing and the timeliness of issuer filings with the SEC.

Review of Engagement Documentation

The review of engagement documentation would be substantially more expansive than currently required and could, in addition to the scope of procedures, present formidable challenges in practice. We believe the resulting delays and costs would greatly exceed the resulting benefit. We suggest the documentation subject to review include memoranda which summarize the relevant engagement matters, such as engagement planning; materiality and risks; significant accounting, auditing and financial reporting matters; high-risk transactions and balances; summary of unadjusted audit differences; management's report on internal control over financial reporting; and audit independence.

Qualifications of the Engagement Quality Reviewer

We agree with the revised guidance in the Proposed Standard requiring that the engagement quality review be performed by a partner in the firm. However, we continue to believe that requiring qualifications identical to those of the engagement partner will unquestionably result in resource constraints, particularly in view of the concurring reviewer rotation requirements. We recommend the Proposed Standard incorporate less prescriptive guidance and allow greater professional judgment in determining the necessary qualifications for the role.

Cost Benefit Considerations

We think the costs under the Proposed Standard do not appear to be reasonable in relation to the benefits to be achieved. Based on discussions with representatives of national public accounting firms, we continue to believe the full cost of these

requirements has been significantly underestimated. In addition to the cost implications, we believe there may be fairly significant resource constraints and timing issues.

Transition

The Proposed Standard would be effective for reports issued after December 15, 2009. We do not believe the proposed transition would afford auditors sufficient time to address the process and resource challenges which the Proposed Standard would entail, particularly in view of the timing surrounding the public exposure process of the PCAOB and SEC. We again recommend these requirements under the Proposed Standard be effective for engagements beginning one year after issuance of the Proposed Standard.

We thank you for the opportunity to express our views in this letter. If you have any questions or would like to further discuss our comments, please feel free to contact me at (703) 641-2385.

Sincerely,

Donald G. DeBuck
Vice president and Corporate Controller

cc: Mr. Mark W. Olson, Chairman
Mr. Daniel L. Goelzer, Board Member of the PCAOB
Mr. Bill Gradison, Board Member of the PCAOB
Mr. Charles D. Niemeier, Board Member of the PCAOB
Steven B. Harris, Board Member of the PCAOB
Mr. Thomas Ray, Chief Auditor

Exhibit 1

**Response to the Questions Set Forth in PCAOB Release No. 2009-001,
“Proposed Auditing Standard – Engagement Quality Review” (the “Proposed
Standard”)**

1. Should the standard require an EQR for other kinds of engagements performed according to PCAOB standards? If so, what types of engagements should be included and what should an EQR of such engagements entail?

We agree with the Board that engagement quality review should only be required for audits and the review of interim information.

2. Is the objective in the repropoed standard appropriately formulated? Does it articulate the purpose of an EQR?
3. Will the objective contribute to a more thoughtful and effective EQR?

In our view, the objective should be stated more generally. We believe the objective should be to provide reasonable assurance the engagement team has performed their examination in accordance with PCAOB auditing standards, the financial statements are in accordance with generally accepted auditing standards and the audit report is appropriate in the circumstances. This broader approach to the objective would allow a less prescriptive approach with regard to the specific procedures and documentation requirements.

4. Is it appropriate to explicitly require a reviewer in the firm to be a partner or an individual with an equivalent position?
5. Should the standard allow qualified accountants who are not employed by an accounting firm to conduct the review?
6. Should the standard prohibit the engagement partner from serving as the reviewer for a period of time following his or her last year as the engagement partner? If so, is two years sufficient, or should it be extended?

We agree with the revised guidance in the Proposed Standard requiring that the engagement quality review be performed by a partner in the firm. However, we continue to believe that requiring qualifications identical to those of the engagement partner will unquestionably result in resource constraints, particularly in view of the concurring reviewer rotation requirements. We recommend the Proposed Standard incorporate less prescriptive guidance and allow greater professional judgment in determining the necessary qualifications for the role.

7. Are the descriptions of the scope and the extent of EQR procedures contained in the proposed standard appropriate? Will the performance of these procedures result in a high quality audit? If not, how should these procedures be revised?
8. Are the specifically required procedures appropriately tailored to reflect the difference in scope between an audit and an interim review?
9. Do the specifically required procedures sufficiently focus reviewers on areas of high risk? Are there other procedures that should be required?

Procedures required under the Proposed Standard are far more exhaustive than practicable or necessary to achieve the necessary assurance. Review of all high risk areas of the engagement for a global client would not only be duplicative but would likely not be feasible. A scope this exhaustive could potentially require a parallel global engagement team working directly under the supervision of the quality reviewer. This would not only result in substantial additional cost without commensurate benefit but could also significantly and adversely impact audit timing and the timeliness of issuer filings with the SEC.

10. Is the standard for engagement quality reviewer's concurring approval of issuance appropriately described in the repropoed standard? Is the first condition appropriately tailored to reflect the difference between an audit and an interim review?

The standard for the engagement quality reviewer's concurring approval is appropriate and the modification of the first condition concerning sufficient evidence is appropriate in the context of a review of interim financial information.

11. Are the documentation requirements in the repropoed standard appropriate? If not how should they be changed?

The review of engagement documentation would be substantially more expansive than currently required and could, in addition to the scope of procedures, present formidable challenges in practice. We believe the resulting delays and costs would greatly exceed the resulting benefit. We suggest the documentation subject to review include memoranda which summarize the relevant engagement matters, such as engagement planning; materiality and risks; significant accounting, auditing and financial reporting matters; high-risk transactions and balances; summary of unadjusted audit differences; management's report on internal control over financial reporting; and audit independence.



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April 20, 2009

Office of the Secretary
Public Company Accounting Oversight Board
1666 K Street, N.W.
Washington, D.C. 20006-2803

RE: **PCAOB Rulemaking Docket Matter No. 025, *Engagement Quality Review*, PCAOB Release No. 2009-01**

Office of the Secretary:

Crowe Horwath LLP appreciates the opportunity to comment on the Public Company Accounting Oversight Board's ("PCAOB" or "Board") Proposed Auditing Standard, (the "Proposed Standard").

The concurring reviewer responsibility included in the PCAOB's interim standards provides a meaningful periodic objective review of audit process performance and client financial reporting. The concurring review process adds some assurance to audit quality control. We applaud the Board's objective of providing greater clarity to the requirement for such engagement reviews, and believe that one result of clarity will be greater consistency in application both within firms and throughout the profession. The proposed requirement that all registered firms that perform audits of issuers conduct engagement quality reviews is a needed enhancement to the interim standards.

We believe the Board has been responsive to the letters of comment on the previous proposal, and that this Proposed Standard is improved and more appropriate than the previous proposal. However, we believe the Proposed Standard can be further improved.

Objective, paragraph 2

The Proposed Standard indicates that the "...*engagement quality reviewer is to perform an evaluation of the significant judgments made by the engagement team and the conclusions reached in forming...*" We believe insertion of "related" prior to the word "conclusions" in that statement would add clarity to the objective that the engagement quality reviewer is evaluating significant conclusions reached and not all conclusions reached.

Engagement Quality Review for an Audit

The above observation is also applicable in paragraph nine (9) when referring to “conclusions reached” in the first and second sentences. We would recommend inserting “related” in front of “conclusions” thereby clarifying that this only pertains to these significant conclusions and not all conclusions.

In addition, the last sentence in paragraph 9 appears to indicate that the engagement quality reviewer is to “identify” significant judgments by reviewing documentation. It should not be the engagement quality reviewer’s responsibility to identify significant judgments as this would imply a complete review of the working papers. In the release section of this document, the Board indicated several changes were made to this section and as noted on page 17, the new proposal requires the “reviewer to evaluate the significant judgments made by the engagement team”. There is no mention of the responsibility to “identify through review of documentation” significant judgments made by the engagement team. The proposal as drafted would cause significant cost to an engagement for the reviewer to review all documentation to identify significant decisions, therefore, we recommend the deletion of the words “identify and” in the last sentence of paragraph 9.

We would recommend adding to the end of paragraph nine (9) the following for clarity – “as deemed appropriate”, thus the engagement quality reviewer would use their judgment to determine what documentation should be reviewed. As currently drafted, it could be interpreted to be all documentation and we don’t believe that is appropriate.

Paragraphs 10e and 10f require the engagement quality reviewer to “determine” if appropriate matters have been communicated and “determine” if appropriate consultations have taken place. These requirements would assume full knowledge of all the working papers in an audit, because without full knowledge, a reviewer could not determine if the appropriate matters were communicated or if the appropriate consultations have taken place. Clarity can be provided to these steps as follows: “Based on the procedures performed above, evaluate if appropriate matters have been communicated...” We believe the same change could be made to item 10f. In addition, we recommend moving these two procedures to items 10g and 10h, therefore “procedures performed above” would refer to all the procedures in paragraph 10 except the current paragraph 10i that we believe is appropriate to be last.

Documentation of an Engagement Quality Review

Several steps provided in paragraph 19 would add significant cost to the review process without significant benefit. We recommend several changes for clarity which we do not believe reduces the quality of the process. Step b – we recommend inserting “significant” prior to “documents” thus the step would read “The significant documents reviewed by the engagement quality reviewer and others who assisted the reviewer.” In addition, step c – should be deleted as this does not add quality but it will add time. In paragraph 10, the engagement quality reviewer is concluding on various aspects of the engagement based on review of certain documents and discussions with the engagement team. They should be allowed to use their judgment in documenting how they reached their conclusions and what

would be appropriate to document based on AS-3. Step 19c is an unnecessary documentation step to the defined process.

Effective Date

We believe the effective date provided in the Proposed Standard should be changed. Most issuer audit engagements for the current year will have substantial services performed prior to a final standard becoming effective. The changed responsibilities of the engagement quality reviewer would be in effect for services already performed (planning, risk assessments, interim procedures). Firms also need time to implement the new requirements, including training, review of and potentially changing assignment of engagement quality reviewers to be compliant with new requirements. We suggest that the effective date be for periods beginning on or after six months after a final standard is approved by the SEC and in no event earlier than fiscal years beginning on or after December 15, 2009.

Release, item E Concurring Approval of Issuance – “know or should have known”

Though the Board removed “know, or should have known” from the revised proposed standard text, the Board’s conclusion in the release document that the requirement to exercise due professional care imposes on a reviewer essentially the same requirement as know, or should have known, suggests a new standard of performance for an engagement quality reviewer. Such a new standard requiring “know or should have known” would be a significant increase in the level of responsibility for a reviewer. To perform at this level the reviewer will need to develop knowledge and judgment comparable to a second engagement partner.

The focus of an engagement quality review standard should be on reviewing the significant judgments made and conclusions reached by the engagement team, not on developing a second set of independent conclusions. The expansion of the definition of “due professional care” by the Board noted above to a “know or should have known” level of performance changes the nature of the review from negative assurance to positive assurance by the reviewer. The focus on independent evaluations and positive assurance turns the focus of the audit to the engagement quality review rather than on the conclusions and judgments of the engagement team.

The engagement partner must have the ultimate responsibility for the audit. The engagement quality reviewer should not become an integral part of the engagement team, and should not have a level of responsibility comparable to the engagement partner, including overall responsibility for the audit. Unlike the engagement team members, the engagement quality reviewer's access to client records is limited, and they likely do not have routine interaction with the client. The need for independence and objectivity in this function, as well as the practical limitations on the scope of the engagement quality review, prevent the reviewer from forming the necessary judgments and conclusions to re-perform many of the evaluations and decisions made during the audit.

We recommend that the Board eliminate this concept of “know or should have known” as inclusion adds a new concept and reduces clarity.

* * * * *

Crowe Horwath LLP supports the Board's efforts to improve its auditing standards with the objective of furthering the public interest. We hope that our comments and observations will assist the Board in its consideration of the Proposed Standard. We would be pleased to discuss our comments with members of the Public Company Accounting Oversight Board or its staff. If you have any questions on our comments, please contact Wes Williams or Mike Yates.

Cordially,

A handwritten signature in cursive script that reads "Crowe Horwath LLP". The signature is written in black ink and is positioned below the word "Cordially,".

Crowe Horwath LLP



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March 2, 2009

Public Company Accounting Oversight Board
Office of the Secretary
1666 K Street, N.W.
Washington, D.C. 20006-2803

Re: PCAOB Open Meeting to Consider Reproposing an Auditing Standard on Engagement Quality Review

Dear Sir:

Deloitte & Touche LLP (“D&T”) commends the decision of the Public Company Accounting Oversight Board (the “Board” or the “PCAOB”) to discuss in an open meeting on March 4, 2009 its consideration of reproposing its proposed auditing standard on engagement quality review (“EQR”). We believe that reproposing the EQR auditing standard, reflective of the concerns articulated in the extensive comments the Board received on the original proposed standard, and on which the public would have the opportunity to comment, will promote the development of quality standards, and lead to a better understanding and application of standards receiving final approval.

In our letter to the Board dated February 18th, 2009 (see pp. 5, 17-18) commenting on the Board’s *Proposed Auditing Standards Related to the Auditor’s Assessment of and Response to Risk and Conforming Amendments to PCAOB Standards* (PCAOB Release No. 2008-006, October 21, 2008, PCAOB Rulemaking Docket Matter No. 026), as well as in previous letters to the Board, we have discussed the critical importance of transparency in the Board’s standard-setting process, which we feel is fostered by having a second exposure draft of proposed standards if significant comments are received.

As such, we strongly encourage the Board during its open meeting to vote in favor of reproposing its revised EQR auditing standard and seeking public input on the revised EQR proposal.

If you have any questions or would like to discuss these matters further, please do not hesitate to contact James Schnurr at (203) 761-3539 or John Fogarty at (203) 761-3227. We thank you for your consideration of these comments.

Very truly yours,

/s/ Deloitte & Touche

cc: Mark W. Olson, PCAOB Chairman
Daniel L. Goelzer, PCAOB Member
Bill Gradison, PCAOB Member
Steven B. Harris, PCAOB Member
Charles D. Niemeier, PCAOB Member
Thomas Ray, Chief Auditor and Director of Professional Standards



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April 20, 2009

Office of the Secretary
PCAOB
1666 K Street, N.W.
Washington, D.C. 20006-2803

**Re: PCAOB Rulemaking Docket Matter No. 025
Proposed Auditing Standard – Engagement Quality Review**

Deloitte & Touche LLP (“D&T”) is pleased to respond to the request for comments from the Public Company Accounting Oversight Board (the “PCAOB” or the “Board”) on its *Proposed Auditing Standard on Engagement Quality Review*, PCAOB Rulemaking Docket Matter No. 025 (Mar. 4, 2009).

If you have any questions or would like to discuss these issues further, please contact Jim Schnurr at 203-761-3539.

Very truly yours,

/s/ Deloitte & Touche LLP

cc: PCAOB
Mark W. Olson, Chairman
Daniel L. Goelzer, Member
Bill Gradison, Member
Steven B. Harris, Member
Charles D. Niemeier, Member

SEC
Mary L. Schapiro, Chairman
Luis A. Aguilar, Commissioner
Kathleen L. Casey, Commissioner
Troy A. Paredes, Commissioner
Elisse B. Walter, Commissioner

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I. INTRODUCTION

Deloitte & Touche LLP (“D&T”) appreciates the opportunity to provide comments on the PCAOB’s proposed standard on engagement quality review (“EQR”) (*Proposed Auditing Standard on Engagement Quality Review*, PCAOB Rulemaking Docket Matter No. 025 (Mar. 4, 2009) (the “Revised Proposal”). We applaud the PCAOB’s decision to re-propose the EQR standard and invite additional public comments, given both the importance of the standard itself and the extensive scope of comments on and numerous changes made to the original proposed standard (*Proposed Auditing Standard on Engagement Quality Review*, PCAOB Rulemaking Docket Matter No. 025 (Feb. 26, 2008) (the “Original Proposal”). We believe allowing for a second round of public comments enhances the transparency of the Board’s standard setting process and promotes the development of high quality standards.

As explained in our comments on the Original Proposal, D&T strongly supports the function of EQR and is committed to an effective EQR process that promotes audit quality. D&T supports several key improvements made in the Revised Proposal, including the adoption of an objective for the overarching framework of EQR, and the addition of a separate EQR process for reviews of interim financial information. We appreciate the consideration that was given to our previously submitted comments, as several of the changes that were adopted provide additional clarity and will help facilitate proper implementation of the EQR standard when finalized.

As explained below, we have several significant concerns with the Revised Proposal that we believe must be addressed to help provide for an effective and appropriate EQR standard. D&T’s comments on the Revised Proposal reflect the judgment and experience of numerous partners within D&T, including a significant number of partners who currently perform EQRs.

We first provide general comments on the Revised Proposal, and then provide responses to specific questions contained in the Release. In so doing, we suggest alternatives that we believe should be effective in promoting audit quality through EQR, while avoiding costly and unwieldy implementation problems. These suggested changes are described below and are also set forth in a copy of the Revised Proposal marked to show proposed changes in blackline, attached as an Appendix.

II. GENERAL COMMENTS

A. **The EQR Standard Should Reflect The Important, But Limited, Purpose Of Concurring Review As A “Second Look” At The Engagement.**

In the context of conducting an audit (or interim review), we recognize that concurring review plays an important role. Its purpose, as noted in the Release to the Original Proposal at page 2, is to provide an “objective ‘second look’ at the engagement.” In addition to the EQR, it is important to bear in mind that there are multiple layers of review that are performed by the audit engagement team and multiple layers of quality controls within the firm. The EQR is a supplemental layer of quality control, but it is not intended to duplicate other reviews performed by members of the engagement team or replace other controls embedded within the audit

process. Accordingly, the “second look” is limited by design: “a concurring reviewer is not expected to do the audit all over again.”¹

We support the adoption of an EQR standard that aligns with the intended role of EQR as a second-look review, and is not duplicative of other elements of the audit process or the quality control systems of the firm. To this end, we believe the final standard should encourage the exercise of professional judgment by EQR reviewers in conducting reviews. Such a principles-based approach would result in higher quality audits because EQR reviewers – who are highly skilled and knowledgeable individuals – could approach the review based on the facts and circumstances presented by each engagement, and could use their seasoned judgment in determining which areas of the engagement require more attention. In contrast to this principles-based approach, establishing overly prescriptive procedures and requirements for EQRs would likely lead to a “check-the-box” approach that places undue emphasis on performing and documenting procedures in order to demonstrate compliance with the EQR standard. Although the checklist approach may facilitate after-the-fact review, it would not serve the goal of audit quality.

EQRs are particularly ill-suited for this type of mechanical exercise because these reviews inherently involve a significant degree of professional judgment. EQR reviewers provide a high-level review of the engagement team’s work, which cannot be readily encapsulated through a formulaic review process. EQR reviewers must be afforded the discretion to navigate through the overall engagement and select which areas of the engagement team’s work would most likely benefit from additional scrutiny. The EQR is not intended to replicate the work of the engagement team; rather, it is intended to provide a second review that allows the EQR reviewer to understand and concur with the overall conclusion of the audit based on the significant judgments made and related significant conclusions reached by the engagement team.

It is with this framework in mind that we make many of the specific comments below. Many of these suggestions relate directly to the intended focus of the EQR as a second-look review, and the need to adopt a principles-based approach that allows for the appropriate use of professional judgment by the EQR reviewer in conducting the review.

B. The PCAOB Should Adopt An EQR Standard That Is Consistent With Prevailing International Standards.

There are significant advantages that may be realized with increased convergence of global standards. The Board’s Strategic Plan states its intention to benefit from the work of other standard setters and professional bodies and to leverage best practices and other auditing enhancements made by the International Audit and Assurance Standards Board (“IAASB”) and

¹ *Potts v. SEC*, 151 F.3d 810, 813 (8th Cir. 1998).

the Auditing Standards Board (“ASB”).² We appreciate the steps that have been taken toward convergence in the Revised Proposal.

The Revised Proposal, however, in some areas uses terminology and imposes requirements that are not contained in – and are seemingly inconsistent with – the international standards. This is not to say that convergence should be pursued indiscriminately. We recognize – and agree – that the EQR standard must reflect unique aspects of the regulatory and legal regime present in the United States that may require variance from international standards. For example, we explain below that wholesale adoption of international standards in Paragraph 10(c) is not appropriate, because independence requirements are significantly more intricate in the context of the regulatory environment that exists in the United States. Therefore, the PCAOB should be mindful of these important considerations when incorporating aspects of international standards. Where there is room to achieve convergence without encroaching upon such important policy concerns, however, we encourage the PCAOB to do so in adopting the final standard.

1. Converging Standards Should Improve The Performance Of EQRs.

Building upon well-understood international standards for EQR, while departing where appropriate, will improve the quality of EQRs. Convergence also would facilitate the performance of quality EQRs because having a common framework of standards promotes a better understanding among auditors of the required procedures. Many firms develop their audit methodologies based on the ISAs, and for that reason are already quite familiar with the provisions therein. Ensuring that PCAOB requirements concerning EQRs are clear and consistent with the existing ISA standards will improve the overall understanding of what is expected for EQRs performed for public companies listed in the United States. Moreover, making sure that any PCAOB-specific requirements are obvious will make it easier for other countries (and the IAASB) to consider adding the same requirements.

2. In The Process For Adopting Audit Standards, The PCAOB Should Look To International Standards.

In this comment letter we have focused on providing specific comments related to the Revised Proposal. We also would like to reiterate, however, some of the broader points about setting audit standards that we made in our letter dated February 18, 2009 in response to the PCAOB’s request for comments on the *Proposed Auditing Standards Related to the Auditor’s Assessment of and Response to Risk and Conforming Amendments to PCAOB Standards*, PCAOB Rulemaking Docket Matter No. 026 (Oct. 21, 2008) (“Proposed Risk Assessment Standard”).

In order to benefit from existing standards and avoid unnecessary differences with them, the PCAOB should establish a standard-setting process whereby it uses the language in the ISAs

² PCAOB Strategic Plan 2008-2013, at 10 (Mar. 31, 2008).

(which are developed with PCAOB input) as the starting point (i.e., the “base”), and then expressly modifies this language as the PCAOB determines necessary for audits of SEC issuers. Using the ISAs as a base will help avoid unintentional changes in practice, make the intentional changes obvious to all interested parties, and make comparability between the standards more apparent – all of which will help auditors in applying the standards.

This approach would be beneficial because it is unclear in several instances whether the Revised Proposal presents a requirement that the PCAOB intends to be different from the ISAs, or that it intends to have the same meaning. This concern is particularly acute when the Revised Proposal seems to be referring to or explaining the same process or concept as the ISAs, but uses different terminology to do so. Specific examples are addressed below in analyzing EQR procedures required under Paragraphs 9, 10, and 15. Using terminology that is different from the ISAs adds significantly to the complexity of the EQR standard, challenging auditors to interpret what exactly is required and how it may differ from procedures performed when applying the ISAs. These differences could adversely affect audit quality and efficiency.

With regard to the Revised Proposal, we believe that much-needed clarity and guidance would be provided to the audit profession if the final standard included a comparison of its provisions to the current interim EQR standard and to the ISA. The PCAOB is certainly familiar with the utility of this approach as the recently Proposed Risk Assessment Standard included a general comparison with international standards. We believe this approach enhanced the public’s understanding of the Proposed Risk Assessment Standard, and believe that similar benefits would be realized by including such comparisons when the final EQR standard is adopted.

In addition, we recommend that the PCAOB issue separate standards pertaining to quality control policies and procedures rather than embody such requirements in audit standards. As noted below in the discussion of Paragraph 4, there are instances in this Revised Proposal where the proposed standard appears to intertwine the substance of the EQR standard with quality control policies and procedures designed to achieve compliance with the standard. The international standards, as well as the PCAOB interim standards, have separate standards for each. This structure provides greater clarity, and should be considered by the PCAOB, with respect to the current standard-setting effort.

III. CONCERNS WITH SPECIFIC PROVISIONS AND RESPONSES TO QUESTIONS IN THE RELEASE

In this section, we provide comments on specific paragraphs of the Revised Proposal, as well as responses to several of the specific issues on which the PCAOB has sought comments. Our comments are presented in the order of relative significance, beginning with our more significant concerns.

A. The Proposed “Due Professional Care” Reference Is Not Appropriate.

Question No. 10. Is the standard for the engagement quality reviewer’s concurring approval of issuance appropriately described in the reproposed standard?

Although revised from the Original Proposal, the standard set forth in Paragraph 12 (as well as in Paragraph 17, in relation to interim reviews) still presents significant concerns.

The Original Proposal would have required the EQR reviewer to make a concurring approval based on what he or she “knows, or should know.” In our comment letter on the Original Proposal, we objected to this standard and explained its illogic and unfairness. Paragraph 12 of the Revised Proposal has removed the “knows, or should know” standard and instead provides that an EQR reviewer “may provide concurring approval of issuance only if, after performing with due professional care the review required by this standard, he or she is not aware of a significant deficiency.”

Removing the inappropriate and unworkable “knows, or should know” formulation from the text of Paragraph 12 is a positive step. Unfortunately, any improvements from removing the “should know” formulation are substantially offset by the statement in the Release at page 24 that “the requirement to exercise due professional care imposes on a reviewer essentially the same requirement as the ‘knows, or should know based on the requirements of this standard’s formulation in the Board’s original proposal.” Further, we believe that inclusion of the legal standard of “due professional care” in the EQR standard itself presents concerns, separate and apart from the Release’s interpretation that it equates to a “should know” requirement.

1. The Inclusion Of A Legal Standard Is Inappropriate In An Audit Standard.

As an initial matter, the PCAOB should not include the concept of “due professional care” in this standard. Legal standards are not appropriate for explicit inclusion in audit standards; yet this is precisely what is done in Paragraphs 12 and 17.

As noted in the Release at page 23, AU sec. 230 imposes a general duty upon auditors to perform audit work with “due professional care.” The PCAOB thus acknowledges that auditors are currently subject to a due professional care requirement, and, therefore, inclusion of this legal standard in the final EQR standard is unnecessary. Other audit standards do not contain an explicit requirement of “due professional care.” It would be problematic to single out the EQR process, generally, and the issuance of a concurring approval, specifically, as being subject to a standard of due professional care – suggesting, perhaps, that the EQR standard is somehow different in this regard from other audit standards; or that the absence of an explicit invocation of due professional care in other standards must be given meaning. On this ground alone, the “due professional care” reference should not be included in the final standard.

2. If “Due Professional Care” Is Nonetheless Included In The Final Standard, The “Knows, Or Should Know” Interpretation Should Be Explicitly Rejected.

The interpretation of due professional care on page 24 of the Release as “essentially the same requirement” as the “knows, or should know” formulation from the Original Proposal creates additional concerns. As we discussed in our comment letter on the Original Proposal, the “should know” standard is illogical – and thus unworkable – in this context because a reviewer cannot reasonably be expected to provide a concurring approval based on what he or she “should know,” as opposed to what the reviewer actually knows. Adoption of this standard would have

created an undue incentive to perform additional procedures due to concerns of second-guessing by others about information that the EQR reviewer should have known. Such protective procedures would add disproportionately to the time and effort involved with the EQR and ultimately to audit costs. For example, the reviewer may believe it is necessary to perform a detailed review of all of the audit working papers to meet the “should know” standard. This would appear to be illogical and inconsistent with the objective of a review that is focused on the significant judgments made and the related significant conclusions reached by the engagement team.

Moreover, what the EQR reviewer “should know” could well be construed to impose a threshold that is unrealistic, and even higher than the general interpretation of due professional care, as it is well recognized that “even an audit conducted in strict accordance with professional standards countenances some degree of calibration for tolerable error which, on occasion, may result in a failure to detect a material omission or misstatement.”³ The “should know” standard could be interpreted as requiring the EQR reviewer to be familiar with every conceivable aspect of an audit, going far beyond an appropriate use of professional judgment (and due professional care) in conducting a second-look review.

An EQR reviewer confronted with the potentially unbounded scope of the “should know” formulation could reasonably construe the requirement as meaning that he or she must have the same – if not a greater – level of knowledge and understanding regarding the client and be in a comparable position as the engagement partner in order to draw the required conclusions. The burden it would impose on EQR reviewers could be prohibitive and inconsistent with the current understanding of the EQR as a “second look.”

Finally, equating due professional care to what the reviewer “should know” is incongruent with the last part of Paragraph 12, which specifies that after performing the EQR, the reviewer “is not aware of a significant engagement deficiency.” In that regard, Paragraph 12 specifies that the EQR reviewer provides the concurring approval based on what he or she is *actually* “aware of.” Yet, at the same time, by embracing an overly expansive interpretation of due professional care, the Release suggests that the EQR reviewer is also responsible for matters that he or she *should have known*. This plain conflict will undoubtedly cause significant confusion and uncertainty in implementation.⁴

³ *In re Ikon Office Solutions, Inc.*, 277 F.3d 658, 673 (3d Cir. 2002) (explaining that “audit requires only due professional care”).

⁴ We note that the PCAOB has traveled down this path before in a separate rulemaking, *Ethics and Independence Rules Concerning Independence, Tax Services, and Contingent Fees*, PCAOB Rulemaking Docket Matter No. 017 (Jul. 26, 2005). The PCAOB considered a “should have known” standard with regard to the provision that an associated person of an audit firm not cause the firm to commit an ethical violation. As described on pages 9 through 14 of the Release to the final rule, however, the PCAOB ultimately decided against adopting the “should have known” formulation, stating, among other things, that it did not want to

[Footnote continued on next page]

3. If “Due Professional Care” Is Nonetheless Included In The Final Standard, The PCAOB Should Clarify That In This Context, “Due Professional Care” Is Not A Negligence Standard.

The proper meaning of “due professional care” can be a difficult legal question that the PCAOB may not wish to address or undertake to resolve in the context of establishing the new EQR standard. As set forth above, there are persuasive reasons for not including “due professional care” in the standard, independent of any dispute about legal interpretation of the phrase. But if the final standard does retain a reference to “due professional care,” the Board should clarify that in the context of EQR, this phrase is not intended to impose liability based on mere negligence.

The Release cites only one case on this issue, *Potts v. SEC*, 151 F.3d 810 (8th Cir. 1998). But *Potts* does not stand for the proposition that due professional care imposes a negligence standard. *Potts*, in fact, applied a *recklessness* standard, concluding that the concurring reviewer “had acted with reckless disregard of his duties as an independent auditor.”⁵ The standard for recklessness, as applied to the concurring reviewer in *Potts*, was whether the reviewer’s conduct constituted an “egregious refusal to see the obvious, or to investigate the doubtful.”⁶ Therefore, *Potts* did not equate due professional care owed by the concurring reviewer with negligence, as suggested by the Release. Rather, *Potts* simply held that concurring reviewers may be sanctioned for conducting reviews in a reckless manner.

Further, courts interpreting and applying a legal standard of due professional care recognize that audit professionals exercise professional judgment in discharging their duties and that the analysis is more nuanced than simply equating due professional care to negligence. The fact that one or more of the professional judgments made by an auditor in conducting a review may have been in error does not by itself render the audit work performed defective or breach the standard of due professional care. The court in *Mishkin v. Peat, Marwick, Mitchell & Co.*, 744 F. Supp. 531, 538 (S.D.N.Y. 1990), confirmed this view:

An auditor who undertakes to examine the books and audit the accounts of a client does not guarantee the correctness of the accounts. He does undertake to use skill and due professional care and to exercise good faith and to observe generally accepted auditing standards and professional guidelines, with the appropriate reasonable, honest judgment that a reasonably skillful and prudent auditor would use under the same or similar circumstances. He is not responsible

[Footnote continued from previous page]

sanction individuals “who act in an appropriate, reasonable manner that, in hindsight, turns out to have not been successful.” These same reasons caution restraint here as well.

⁵ *Potts*, 151 F.3d at 812.

⁶ *Id.* (citation omitted).

for mere error of judgment. Reasonable adherence to the standards is a matter calling for application of experience, skill and the exercise of independent judgment. The standards concern themselves not only with the auditor's professional qualities but also provide that judgment may be exercised by him in the performance of his examination and in his report. Deviation from standards does not perforce thereof spell negligence in an audit, nor are innocent blunders culpable fault.

This legal framework is not mentioned in the Release, which only adds to the uncertainty surrounding the purported meaning of “due professional care” in Paragraphs 12 and 17.

Moreover, there is an even more fundamental concern with the Revised Proposal's approach. The courts view due professional care in this context as characterizing the degree of departure from an underlying audit standard, not conduct that is prescribed by the standard itself. If required procedures for reaching an EQR conclusion are defined through the prism of due professional care, it is unclear how this affects the legal standard that the PCAOB will apply in assessing whether an auditor failed to comply with the audit requirements. Under the Sarbanes-Oxley Act of 2002, many of the sanctions that may be imposed against auditors for violating audit standards apply only to reckless conduct, or repeated instances of negligent conduct, in deviating from an applicable audit standard.⁷ It would therefore be inconsistent with this statutory framework to impose indirectly a different liability standard – negligence, to the extent that the PCAOB interprets due professional care to be a negligence standard – through the EQR standard. This would be especially problematic because efforts could be made to invoke the different liability standard in private claims brought against auditors – this would conflict with Sarbanes-Oxley. Moreover, it would be a role ill-suited for the PCAOB to take upon itself to create standards of liability for private causes of action.

For all of the reasons noted above, we strongly urge that the PCAOB omit any reference to “due professional care” in the final standard. If for some reason, the reference is retained, the Board should explicitly disavow any intent to equate the legal standard with a “knows or should know” negligence standard in the EQR context.

4. Paragraph 12 Should Be Aligned With The Stated Objective Of EQRs And International Standards.

We suggest that the PCAOB adopt the following language, which retains the structure of Paragraph 12 from the Revised Proposal, but narrows the scope of the EQR reviewer's determination to the significant facts that have come to the reviewer's attention during the EQR:

In an audit, the engagement quality reviewer may not provide concurring approval of issuance if, after performing the review required by this standard, he or she is aware that (1) the engagement team failed to obtain sufficient appropriate

⁷ 15 U.S.C. § 7215(c)(5).

evidence in accordance with the standards of the PCAOB, (2) the engagement team reached an inappropriate overall conclusion on the subject matter of the engagement, or (3) the engagement report is not appropriate in the circumstances.

This formulation is consistent with international standards, as well as current practices, that base the EQR reviewer's conclusion on what the reviewer actually knows based on the procedures performed.⁸ Moreover, this recommended language – by removing the reference contained in the Note to Paragraph 12 to whether the firm is independent of its client – is more consistent with the stated objective of EQR, which Paragraph 2 describes as a review of the significant judgments and related significant conclusions reached by the engagement team. In addition, the EQR reviewer, in considering whether the engagement report is appropriate in the circumstances as required under Paragraph 12 above, will also take into consideration whether he or she is aware that the firm is not independent of its client.

B. Portions Of The Revised Proposal Could Be Read To Expand EQR Beyond Its Intended Scope.

Question No. 7. Are the descriptions of the scope and extent of EQR procedures contained in the proposed standard appropriate? Will the performance of these procedures result in a high-quality EQR? If not, how should these procedures be revised?

The scope and extent of the procedures contained in the Revised Proposal could result in substantial changes to the scope and manner in which concurring reviews are currently conducted. As an initial matter, use of the words “evaluate” and “determine” in the context of the EQR could be viewed to require the EQR reviewer, among other things, to undertake extensive procedures beyond those intended by the Board, particularly in light of the broadly described “reviewing documentation” requirement in Paragraph 9. Some aspects of the specified EQR procedures in Paragraphs 9 and 10 are inconsistent with the stated objective contained in Paragraph 2 – i.e., that an EQR should provide a review of the “significant judgments made by the engagement team” and the related significant “conclusions reached.” Further, some of the procedures for EQR related to interim reviews are inconsistent with the scope of the work performed in a review of interim financial information. These concerns can be readily addressed.

⁸ Redrafted Int'l Standard on Auditing 220, *Quality Control for an Audit of Financial Statements* (Int'l Auditing & Assurance Standards Bd. 2008) (“ISA 220 (R)”), par. 25; Redrafted Int'l Standard on Quality Control, *Quality Control for Firms that Perform Audits and Reviews of Financial Statements, and Other Assurance and Related Services Engagements* (Int'l Auditing & Assurance Standards Bd. 2008) (“ISQC 1 (R)”), par. 42 (“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 it reached were not appropriate.”).

1. The Standard Should Use Clear Language Consistent with EQR’s Function

EQR is intended to be a second-look review of the engagement team’s work and not a re-audit, and the terminology used to describe the EQR process should be consistent with this concept throughout the final standard. In several instances, the Revised Proposal uses terms such as “evaluate”⁹ and “determine”¹⁰ when describing what is required of the EQR reviewer. It is not clear how “evaluate” is different from “determine” and what sort of procedures the EQR reviewer must perform to satisfy the requirements imposed by the use of either term. “Determine” can be defined as “[t]o decide or settle . . . authoritatively and conclusively,” and “evaluate” as “[t]o determine or fix the value of.”¹¹ These concepts are at odds with the intended function of EQR, because they suggest that the EQR reviewer should “decide authoritatively” matters related to the audit, rather than perform a more limited, second-look review of the engagement team’s significant judgments and related significant conclusions.

Given the more definitive inference these terms create, EQR reviewers may feel compelled to perform a broad array of unnecessary procedures in order to obtain more and more information to satisfy themselves that they have done enough to perform the proposed “evaluation” or make the proposed “determination.” As discussed further below, this concern is made more acute by the fact that Paragraph 9, in providing an overarching framework for the procedures to be performed under Paragraph 10, imposes an overly broad requirement of “reviewing documentation,” without providing any guidance concerning the extent of this review. As a result of the expansive manner in which these terms may be construed – especially in conjunction with one another – the time, effort, and resources spent on the EQR could be greatly increased, presumably beyond what the PCAOB intended when it stated in the Release at pages 3-4 that “an effective review need not – and should not – amount to a re-audit, and that the role of a reviewer differs significantly from that of an engagement partner.”

To clarify this issue, we identify specific recommendations below in context of the applicable paragraphs from the Revised Proposal.

2. Paragraph 9 Requires Clarification Concerning The Scope Of Review.

Paragraph 9 provides that the EQR “should evaluate the significant judgments made by the engagement team and the conclusions reached in forming the overall conclusion on the engagement and in preparing the engagement report.” This language requires clarification to achieve its intended purpose, stated in the Release at page 17, “that the reviewer performs the EQR by reviewing the engagement team’s work, rather than by auditing the company himself or herself.” First, for the reasons discussed above, the word “review” should be used instead of

⁹ This term is used in Paragraphs 2, 9, 10, 11, 14, 15, and 16.

¹⁰ This term is used in multiple instances in Paragraph 10.

¹¹ Webster’s II New College Dictionary 315, 395 (3d. ed. 2005).

“evaluate.” Second, the words “related significant” should be inserted before “conclusions reached” to link such conclusions to the “significant judgments.” This concern applies to Paragraph 2, as well, where the same language is used. Otherwise, Paragraphs 2 and 9 could be read to require the EQR to consider non-significant conclusions made by the engagement team, an anomalous result outside the intended scope of an EQR.

Third, as noted above, in considering the significant judgments and conclusions made by the engagement team, Paragraph 9 specifies that the EQR reviewer should perform the procedures described in Paragraph 10 by, among other things, “reviewing documentation.” This requirement is too open-ended and could be interpreted to require an extensive review of audit documentation. There is no guarantee that this language would not necessitate review of the entire complement of an audit’s underlying working papers – an undertaking that is contrary to basic precepts of concurring review and the Board’s stated intent.¹² The PCAOB should modify the final standard to make it clear that the EQR reviewer should exercise professional judgment in determining the scope of review of documentation. To accomplish this purpose, we recommend that the scope of the documentation requirement in Paragraph 9 be restated in the following manner: “reviewing selected documentation as considered appropriate by the engagement quality reviewer.” This would properly express the scope of document review for an EQR in a manner consistent with international standards.¹³

3. Paragraph 10 Requires Clarification Concerning The Scope Of EQR Procedures To Be Performed.

Paragraph 10 of the Revised Proposal sets forth enumerated procedures that EQR reviewers are expected to perform as part of conducting the EQR. Many of these procedures, however, are vaguely described and are not appropriately linked to the stated objective of EQR. In the face of this uncertainty, EQR reviewers may feel compelled to perform a myriad of procedures that the standard could be interpreted to require, and thereby unnecessarily expend time, effort, and resources on an EQR that goes well beyond what the PCAOB may have intended. To avoid these concerns, we offer the following suggestions.

As an initial matter, and as discussed above, we have concerns regarding the use of the words “evaluate” and “determine” as used throughout Paragraph 10, and recommend substituting the language presented in the Appendix to address these concerns. Second, Paragraph 9 should establish the overarching standard of the EQR procedures to be performed; Paragraph 10 should

¹² During the Board’s open meeting on March 4, 2009 to discuss the Revised Proposal, Board Member Goelzer asked a question regarding documentation requirements and during the exchange, a PCAOB staff person stated that the engagement quality reviewer is expected to review “selected documentation.”

¹³ ISA 220 (R), par. 20; ISQC 1 (R), par. 37 (specifying “[r]eview of selected audit documentation relating to the significant judgments the engagement team made and the conclusions it reached”).

then specify specific procedures that the EQR reviewer, in exercising his or her professional judgment, may consider in conducting the review. This approach is consistent with international standards, whereby specific EQR procedures are phrased as guidance, and is also in accord with the notion of EQR as a “second-look” review of the engagement team’s work. To achieve this much-needed clarity concerning the scope of the EQR as well as the use of professional judgment by the EQR reviewer, we recommend rephrasing the beginning of Paragraph 10 in the following manner:

In reviewing the significant judgments and related significant conclusions referenced in Paragraph 9, the engagement quality reviewer, as he or she deems appropriate, may:

Turning to the specific procedures contemplated by Paragraph 10, we have some additional suggestions. First, the various procedures specified in paragraph 10 are not linked to the stated objective of EQR (including as restated in paragraph 9) that the review relate to the “significant judgments made by the engagement team and the [related significant] conclusions reached.” In conformity with the intended scope of the EQR, we believe that the subsections in Paragraph 10(a), (b), and (d) should be modified to make clear that these required procedures are intended to apply to the “significant judgments made by the engagement team and the related significant conclusions reached.” Otherwise, these provisions could be read to require EQR procedures well beyond the objective stated in Paragraphs 2 and 9. We also recommend that the language in Paragraph 10(a) concerning consideration of “risks identified in connection with the firm’s client acceptance and retention process” be deleted because it is already encompassed by the risk assessment language set forth in Paragraph 10(b). Having these duplicative provisions creates unneeded ambiguity about their intended scope.

Second, Paragraph 10(c) specifies that the EQR reviewer should “[r]eview the engagement team’s evaluation of the firm’s independence in relation to the engagement.” We recognize that international standards include a similar requirement under ISA 220 (R), par. 21; ISQC 1 (R), par. 38, but independence requirements in the United States’ regulatory environment are more intricate. Within this context, the engagement team performs certain procedures regarding independence matters (for instance with respect to monitoring the scope of services provided). However, many of the independence issues are monitored through the audit firm’s centralized independence compliance processes. Therefore, we recommend modifying Paragraph 10(c) to limit the scope of the EQR reviewer’s consideration of independence to written communications that the engagement team had with the client under PCAOB Rule 3526 and other relevant issues that come to the attention of the EQR reviewer in performing the procedures specified under Paragraph 10.

Third, under Paragraph 10(d), the EQR reviewer is to consider judgments about “the severity and disposition of identified control deficiencies.” However, there may be a large number of such deficiencies for any individual audit client, especially for large multinational companies. Therefore, the scope of review should be clarified under Paragraph 10(d) as pertaining to “significant deficiencies and material weaknesses” in controls. This suggested change would clarify that the EQR reviewer should focus on material issues related to internal control evaluations.

Finally, under Paragraph 10(f), the EQR reviewer is to “[d]etermine if appropriate consultations have taken place on difficult or contentious matters.” We reiterate our general concern with the use of the term “determine,” as explained above. In addition, we believe that the phrase “difficult or contentious” does not provide adequate specificity about which matters are covered. Accordingly, we recommend rephrasing Paragraph 10(f) in the following manner: “Consider whether appropriate consultations have taken place with respect to significant judgments, including conclusions and documentation of such consultations.” Defining the scope of 10(f) in terms of the “significant judgments” has a more objective meaning and should provide further clarity to the EQR reviewer about which matters to review. It also avoids analysis of “difficult/contentious” but trivial matters.¹⁴

4. The Revised Proposal Appropriately Specifies A Separate EQR Process For Reviews Of Interim Financial Information But Some Of The Requirements Need Modification.

Question No. 8. Are the specifically required procedures appropriately tailored to reflect the difference in scope between an audit and an interim review?

We agree with the approach in the Revised Proposal to differentiate between the EQR procedures to be performed for audits of annual financial statements and for reviews of interim financial information. However, we believe that several of the provisions contained in Paragraphs 14 through 17 are inconsistent with the scope of interim reviews. As discussed in PCAOB Interim Standard AU sec. 722.07, interim reviews consist principally of performing certain limited analytical procedures and making limited inquiries. Because several of the procedures set forth in the Revised Proposal are well beyond this limited scope, we offer the following suggestions for the final standard.

First, we reiterate the same concerns discussed above with regards to EQRs for audits that are also applicable to interim reviews, including the specification of EQR procedures that are broader in scope than the stated objective of EQR (Paragraph 15), the use of the words “evaluate” and “determine” (pervasive throughout the standard, including Paragraphs 14 and 15), the overly broad requirement of “reviewing documentation” (Paragraph 14), and the insertion of a due professional care requirement in the text of the EQR approval language (Paragraph 17).

In addition to these common issues, there are other concerns that are specific to the interim review provisions. Paragraph 15(a) instructs the EQR reviewer to “[e]valuate engagement planning” including “[t]he nature of identified risks of material misstatement due to fraud.” Paragraph 16(a) also specifies that the review of engagement documentation should “[i]ndicate[] that the engagement team responded appropriately to significant risks.” In connection with an interim review, the auditor takes risk into account, but does not engage in the

¹⁴ To the extent that the PCAOB does not adopt our suggested changes to paragraphs 9 and 10, we alternatively would recommend that these paragraphs conform with international standards specified in ISA 220 (R), par. 20, A28.

same type of risk assessment performed for an audit. Based on the language in Paragraphs 15(a) and 16(a), the Revised Proposal, however, would seem to require such risk assessments for interim reviews. We do not believe this is the intention of the Board, as this would significantly elevate the review that is currently performed and is inconsistent with PCAOB Interim Standard AU 722.07, 722.11, and 722.12. Accordingly, we recommend modifying the language in Paragraph 15(a) to align with AU sec. 722.11-13, and removing Paragraph 16(a) from the final standard.

In Paragraph 15(b), the Revised Proposal specifies that the EQR reviewer should perform the procedures described in Paragraph 10(c)-(f). We have previously noted why the scope of the second look at compliance with independence requirements needs to be modified for audits, and that concern applies to interim reviews as well. Paragraph 15(b) also would have the EQR reviewer, in connection with an interim review, evaluate judgments described under Paragraph 10(d)(2) for the “severity and disposition of identified control deficiencies.” However, such deficiencies are assessed by the engagement team under AS No. 5, *An Audit of Internal Control Over Financial Reporting That Is Integrated with an Audit of Financial Statements*, as of the end of the fiscal year; therefore, it would be beyond the requirements of AS No. 5 for the EQR reviewer to engage in such a review in the context of an interim review. Accordingly, we recommend deleting Paragraph 10(d)(2) from the scope of the EQR of an interim review.

Turning to Paragraph 15(c), the Revised Proposal specifies that the EQR reviewer should “[r]ead the interim financial information for all periods presented and for the immediately preceding interim period.” This statement is confusing because it is not clear what one would review when performing the EQR for the first quarter (i.e., interim financial information for the fourth quarter is not reported in the same way interim financial information is reported for other quarters). Further, we note that the Revised Proposal does not contain a similar requirement to read prior financial statements in connection with the EQR of an audit. It would be anomalous to impose a more burdensome procedure on interim reviews. We therefore recommend removing the phrase “and for the immediately preceding interim period” from Paragraph 15(c) to avoid any ambiguity.

Paragraph 15(c) also specifies that the EQR reviewer should read the “related engagement report, if a report is to be filed with the SEC.” Although not all interim reports are filed with the SEC, we nevertheless believe this procedure should be performed regardless of whether a report is in fact filed, and accordingly we believe the standard should be strengthened in this manner.

We also have concerns about language describing the results of interim reviews, such as Paragraph 16(b) which specifies that the review of engagement documentation “[s]upports the conclusions reached by the engagement team with respect to the matters reviewed.” The use of the term “conclusions” is appropriate in connection with an audit, but is not well-suited to describe an interim review, as characterized under PCAOB Interim Standard AU sec. 722.07. The PCAOB should refrain from using this term in the final standard to avoid creating confusion regarding the scope of procedures performed in the context of interim reviews (and paragraphs

14 and 15 should be revised accordingly). Similarly, Paragraphs 17 and 18 specify that an EQR reviewer will provide a “concurring approval of issuance.” However, this term is misleading because reports are not required for interim reviews and are often not “issued.”¹⁵ Therefore, we recommend substituting “concurring approval” in lieu of “concurring approval of issuance” to describe more accurately the EQR’s role with respect to an interim review.

Finally, we recommend that the paragraphs relating to the EQR for interim reviews be removed from this standard and instead incorporated into AU sec. 722, *Interim Financial Information*, as a conforming amendment. Placing these paragraphs in AU sec. 722 will make it clear that the scope of the procedures performed remain under the umbrella of the objective of a review of interim financial information (which is much different than the scope and objective of an audit).

C. The Extensive EQR Documentation Requirements Are A Significant Change In Practice And Will Be A Time Consuming And Costly Process Without Commensurate Benefits.

Question No. 11. Are the documentation requirements in the repropoed standard appropriate? If not, how should they be changed?

Paragraph 19 specifies that documentation of an EQR should be included in the engagement documentation and “should contain sufficient information to identify,” among other things, “(b) [t]he documents reviewed by the engagement quality reviewer and others who assisted the reviewer,” and “(c) [t]he significant discussions held by the engagement quality reviewer and others who assisted the reviewer, including the date of each discussion, the specific matters discussed, the substance of the discussion, and the participants.” Although we recognize the need to document audits appropriately, these provisions would significantly and unnecessarily increase the obligations of EQR reviewers by requiring an extensive compilation of audit documentation that is contrary to the basic precepts of EQR and could be duplicative of the documentation already developed and maintained by the engagement team.

With regard to Paragraph 19(b), we are concerned that requiring a detailed and itemized description of “documents reviewed” may lead to a scope of review inconsistent with the intended role of EQR – which is to perform a second-look review of the engagement team’s work. It may well be the case that based on professional judgment, an EQR reviewer concludes that the working papers that are appropriate for a second look are significantly less voluminous than what was reviewed by the engagement team. The EQR reviewer, however, may feel compelled to engage in an unnecessary review of additional documents in order to compile a more “complete” list for purposes of Paragraph 19(b) – efforts that do not add to audit quality. It also would be very burdensome for the EQR reviewer to make such an exhaustive list of the documents reviewed during the EQR process. In order to address these concerns, the PCAOB

¹⁵ This concern applies to Paragraphs 1 and 2 as well where the term “concurring approval of issuance” is used in apparent reference to both audits and interim reviews.

should modify the final standard to make it clear that the EQR reviewer should exercise professional judgment in determining which documents to identify as being “reviewed” in conjunction with documenting the EQR process. Moreover, the scope of this requirement should comport with the stated objective of EQR in Paragraph 2 to consider “significant judgments made by the engagement team and the [related significant] conclusions reached.” To accomplish this purpose, we recommend that Paragraph 19(b) be rephrased in the following manner:

As considered appropriate by the engagement quality reviewer, the documents relating to the significant judgments made by the engagement team and related significant conclusions reached that were reviewed by the engagement quality reviewer and others who assisted the reviewer,

In addition, we recommend modifying Paragraph 19(c). The scope of this requirement is impractical as an EQR reviewer engages in many discussions relating to an EQR, and the reviewer would be hard-pressed to document each and every discussion as it takes place. This could interfere with the effective conduct of the EQR itself. In addition to the burden, it also would in many respects be redundant of engagement documentation already in the audit file. PCAOB AS No. 3 already requires documentation of significant matters. Therefore, the documentation called for under Paragraph 19(c) may be largely duplicative of existing audit documentation on significant matters. To the extent that the overarching intent behind Paragraph 19 is to provide a record of the EQR process, we believe that a more appropriate way to accomplish this purpose is to require documentation under Paragraph 19(c) of “the procedures performed in accordance with this standard.” This would allow for adequate documentation of the procedures performed in connection with the EQR without requiring a detailed summary of each discussion that occurred along the way. This revised Paragraph 19(c), along with subsections (a), (b) as modified above, and (d) – coupled with existing audit documentation requirements – are more than sufficient to meet the stated goal conveyed in the Release at page 26: “to allow both the Board and the firm itself to understand how the review was conducted and how significant issues were resolved.”

We also have a concern with Paragraph 19(d), which requires identification of the date that concurring approval was issued “or, if no concurring approval of issuance was provided, the reasons for not providing the approval.” We are concerned that this provision could be read to require documentation related to EQRs in these situations, even when no audit report is issued. Providing extensive documentation related to an EQR in a situation where no audit report is issued does not appear to serve any purpose.¹⁶ We therefore recommend revising Paragraph 19 accordingly to limit the scope of EQR documentation requirements under these circumstances.

In addition to the suggested changes described above, the PCAOB should provide further clarity, and lessen any undue burden from the audit documentation requirements, by specifying

¹⁶ For example, in instances where the audit is terminated before the EQR is completed, the EQR reviewer should not be expected to create additional documentation following the termination of the review.

in the final standard that “sufficient information to identify” under Paragraph 19 does not require an exhaustive list of documents reviewed and discussions (if Paragraph 19(c) is in fact included in some form in the final standard) with the engagement team, but rather may consist of a general overview of the EQR process that was performed. This approach is consistent with prevailing international standards under ISA 220 (R), par. 25; ISQC 1 (R), par. 42.

D. The Proposed Competence Requirements Of The EQR Reviewer Require Clarification.

We wholeheartedly agree that EQR reviewers should exhibit “competence,” as specified under Paragraph 4. We are concerned that the description of this requirement in the Revised Proposal could lead to confusion and difficulties in implementation. As set forth in Paragraph 5, the EQR reviewer “*must* possess the level of knowledge and competence related to accounting, auditing, and financial reporting *required to serve* as the person who has overall responsibility for the same type of engagement.” (emphasis added). This phrasing could be read to require the EQR reviewer to have the *same* level of competence (including technical expertise, experience with the client, and specialized knowledge) as the engagement partner. As described below, this is problematic, and there are several changes that should be incorporated into the final standard to alleviate these concerns.

First, the Note to Paragraph 4, which refers to the firm’s quality control policies and procedures governing competence, independence, integrity, and objectivity of the EQR reviewer, is the only place in the EQR standard where quality control policies and procedures of the firm are explicitly referenced. We reiterate our general view stated above that quality control policies and procedures should be issued in a separate quality control standard apart from this audit standard. Moreover, the singular reference contained in the Note to Paragraph 4 could be viewed to suggest that other EQR requirements need not be addressed in the audit firm’s quality control policies and procedures. We do not believe this is the intention of the PCAOB. The Note accordingly should be removed from the final standard to avoid this ambiguity.¹⁷

Second, the Release states at page 11 that the standard “does not require the reviewer’s competence to match that of the engagement partner.” Although we endorse this guidance, the actual text of Paragraph 5 could be read otherwise. Accordingly, we recommend that the quoted language from the Release be specifically incorporated into the text of Paragraph 5. We further

¹⁷ Apart from the specific concern about the Note to Paragraph 4, we have a broader structural concern with the use of Notes in the Revised Proposal. We recognize that Notes may be intended to provide clarity to the underlying standard. However, the use of Notes is confusing when it imposes additional requirements, such as when a standard includes unconditional or presumptively mandatory responsibilities within a Note, as is the case with the Note to Paragraph 6. Significant uncertainty also arises when a Note appears to be inconsistent with the related text in the standard. Notes should not be used in this manner to create additional, perhaps even conflicting, responsibilities separate and apart from the standard itself, and we recommend that the final standard eliminate the use of Notes.

recommend changing the phrase describing the EQR reviewer’s competence from required to “serve as the person who has overall responsibility for the same type of engagement” to “accomplish the objective of this standard.” This appropriately characterizes Paragraph 5 in terms of the competencies required to fulfill the role of the EQR reviewer rather than the role of the engagement partner.

Third, Paragraph 5 uses the word “must” in describing the same attributes of competence that Paragraph 4 concurrently requires of an EQR reviewer.¹⁸ Paragraph 4 specifies the broad requisite qualifications of an EQR reviewer while Paragraph 5 provides guidance on how the overarching competence requirements are to be satisfied. The use of language creating unconditional responsibilities in Paragraph 5 could have the unintended consequence of unnecessarily limiting the availability of eligible and qualified EQR reviewers. The use in audit standards of terms identified in PCAOB Rule 3101 as unconditional responsibilities needs to be reconciled with a principles-based approach to setting standards, as contemplated by the Release at page 11, that facilitates the appropriate use of professional judgment by auditors in conducting reviews. We therefore recommend use of the term “should” in lieu of “must” in Paragraph 5 to avoid unnecessary constraints on assigning appropriate EQRs.

Coupled with the change from “must” to “should,” the final standard also should make clear that judgment should be applied in assigning an appropriate EQR reviewer, taking into account the characteristics of the engagement and an individual’s background and experience – and the experience and skill set of the assistants who will support the EQR reviewer in discharging his or her responsibilities. There may be times when an EQR reviewer without substantial knowledge of the industry may be better suited to conduct an EQR – for example, because he or she has particular expertise dealing with the accounting principles or risks of the engagement that are implicated by issues likely to arise in the audit. Footnote 18 from the Release accompanying the Original Proposal conveyed this approach, noting that competence should be assessed “based on the circumstances of the engagement, including the size or complexity of the business.” We recommend that the PCAOB incorporate this same language into the text of the competence standard. This would be consistent with international standards, which provide for more flexibility in selecting EQR reviewers.¹⁹

Adopting these suggested changes – which in some instances merely entails inserting language used in the Release into the standard – would help to ensure that audit firms have sufficient discretion to match the skills of an EQR reviewer with the characteristics and complexity of an audit. This flexibility will preserve a deeper pool of eligible EQR reviewers. This flexibility is especially important given the auditor independence requirements, including the required rotation of audit partners, which effectively limits the pool of available and

¹⁸ As defined in PCAOB Rule 3101, “must” places an “unconditional responsibility” on an auditor to perform the specified requirements.

¹⁹ ISQC 1 (R), par. A42 (“What constitutes sufficient and appropriate technical expertise, experience and authority depends on the circumstances of the engagement.”).

appropriate concurring review partners. Also, restricting this group of reviewers may have a disproportionate effect on smaller audit firms that may lack the personnel and resources to meet overly rigid EQR reviewer competence requirements. Such a result is surely not intended by the PCAOB and should be rectified in the final standard.²⁰

Question No. 4. Is it appropriate to explicitly require a reviewer from within the firm to be a partner or an individual in an equivalent position?

Paragraph 3 states that the EQR reviewer may be a partner or “another individual in an equivalent position,” but does not specify the meaning of this phrase. It is not clear whether this is intended for firms that do not have partners due to their legal structure, or whether it also applies to firms that have partners. If it is intended to apply to firms with partners, it is not clear who would be eligible to serve as an EQR reviewer. That is, it is not clear whether senior personnel in the firm who may otherwise possess the requisite competence, independence, integrity, and objectivity to serve as an EQR reviewer, but who are not partners, would be deemed to be an “individual in an equivalent position.” The final standard should provide further guidance on these issues.

E. Providing An Objective In The Revised Proposal Is A Positive Change, But The Objective Needs Further Clarification.

Question No. 2. Is the objective in the repropoed standard appropriately formulated? Does it articulate the purpose of an EQR?

Question No. 3. Will this objective contribute to a more thoughtful and effective EQR?

We appreciate the adoption of an objective in the Revised Proposal to further an understanding of the other provisions of the EQR standard, and offer the following suggestions to provide further clarity. Paragraph 2 specifies that the “objective of the engagement quality reviewer is to perform an evaluation of the significant judgments made by the engagement team and the conclusions reached in forming the overall conclusion on the engagement and in preparing the engagement report.” Consistent with the description in the Release, we recommend revising this formulation to make it clear that the overarching objective of the EQR reviewer is to “provide an objective second look at the engagement.” In addition, for the reasons explained above, we recommend that the word “reviewing” should be substituted for the phrase “perform an evaluation of,” and that the term “related significant” should be inserted before “conclusions reached” to link such conclusions to the “significant judgments.”

²⁰ To the extent that the Board elects not to adopt our suggested changes described above, another way to lessen the potential burden is to specify that the EQR team collectively may possess the requisite competence, rather than only the designated EQR reviewer. Although this suggested change may present its own challenges, it would still be an improvement over the less flexible standard in Paragraph 5 of the Revised Proposal.

F. The Proposed Effective Date Is Unrealistic And Should Be Modified.

The PCAOB has proposed that the standard be effective for audits of fiscal years ending on or after December 15, 2009. For reviews of interim financial information, the standard would be effective for fiscal years beginning after December 15, 2009. The Release at pages 27-28 explained that the reason that “implementing the new standard on EQRs of interim reviews in 2009 may not be possible [is] because some of the interim reviews will be performed earlier in the year, and registered firms would not have sufficient time for implementation of the new requirements.”

We fully concur that it is important to provide adequate lead time to implement the new EQR standard, but do not believe that the proposed effective date for either audits or interim reviews provides this necessary transition period.

Firms will have to train their partners and professional employees, re-deploy resources, and create the tools necessary to assist in conducting EQRs compliant with the new requirements imposed by this standard. There would not be sufficient time to implement these steps with the proposed effective date for audits and interim reviews, particularly given the uncertain timeframe of when a standard will be approved as final by the SEC and the potential under the Revised Proposal to increase significantly the amount of work performed (including documentation requirements).

In addition, the proposed effective dates overlook the fact that audits are facilitated by procedures performed during the interim reviews. These interim reviews in many respects are important foundational blocks for the audits of the annual financial statements. Therefore, it would be confusing to require the EQR for an audit to be performed under the new EQR standard if concurring reviews for some of the interim reviews for that audit year were performed under the existing standard. It may lead to EQRs reperforming procedures performed for the interim periods, which would be very burdensome and inefficient.

For these reasons, the new EQR standard should apply to fiscal years beginning twelve months after the date the SEC approves the final standard. The EQR for the first quarter of such fiscal year would then be the first performed under the new EQR standard. During the transition period, the PCAOB could encourage early adoption by firms of concurring review procedures consistent with this standard, and set the expectation that auditors would incorporate features of the new EQR standard into their concurring reviews to help ensure their readiness for full implementation when the standard becomes effective. This would allow sufficient lead time for the firms to take necessary measures to comply with the requirements of the standard, would minimize the impact of the other implementation issues addressed herein, and result in an effective and efficient implementation process.

IV. CONCLUSION

D&T supports efforts to strengthen EQR. We appreciate the changes made in the Revised Proposal. However, we believe that further changes are needed concerning the proposed EQR standard.

We recognize that the issues presented herein are complex and may require further discussion to understand fully the implications of particular comments made by us and by other commenters. We encourage the PCAOB to engage in active and transparent dialogue with commenters as the proposed standard is further evaluated and changes are considered. Such a dialogue will facilitate a more complete understanding of the proposed standard and, we believe, will ultimately improve the final standard and the auditor's ability to implement it effectively and efficiently. We would welcome the opportunity to participate in any such process and to further discuss these matters with the Board and its staff.

* * *

Appendix

Auditing Standard No. X

Supersedes SECPS Requirements of Membership § 1000.08(f).

Engagement Quality Review

Applicability of Standard

1. An engagement quality review and concurring approval of issuance are required for each audit engagement and for each engagement to review interim financial information conducted pursuant to the standards of the Public Company Accounting Oversight Board ("PCAOB").

Objective

2. The objective of the engagement quality reviewer is to ~~perform an evaluation of~~ provide an objective second look at the engagement by reviewing the significant judgments made by the engagement team and the related significant conclusions reached in forming the overall conclusion on the engagement and in preparing the engagement report, if a report is to be issued, in order to determine whether to provide concurring approval of issuance.¹

Qualifications of an Engagement Quality Reviewer

3. An engagement quality reviewer may be a partner of the firm that issues the engagement report (or communicates an engagement conclusion, if no report is issued), another individual in an equivalent position in the firm, or an individual outside the firm. The reviewer may use assistants in performing the engagement quality review. The engagement quality reviewer and assistants must be an associated person/persons of a registered public accounting firm.

4. As described below, an engagement quality reviewer must have competence, independence, integrity, and objectivity.

~~Note: The firm's quality control policies and procedures should include provisions to provide the firm with reasonable assurance that the engagement quality reviewer has sufficient competence, independence,~~

¹ In the context of an audit, "engagement report" refers to the audit report (or reports if, in an integrated audit, the auditor issues separate reports on the financial statements and internal control over financial reporting). In the context of an engagement to review interim financial information, the term refers to the report on interim financial information. An engagement report might not be issued in connection with a review of interim financial information. See paragraph .03 of AU section ("sec.") 722, *Interim Financial Information*.

~~integrity, and objectivity to perform the engagement quality review in accordance with the standards of the PCAOB.~~

5. *Competence.* The engagement quality reviewer ~~must~~should possess the level of knowledge and competence related to accounting, auditing, and financial reporting that is required to serve as the person who has overall responsibility for the same type of engagement.²accomplish the objective of this standard. This does not require the reviewer's competence to match that of the engagement partner. The judgment as to what constitutes the appropriate level of knowledge and competence should be based on the circumstances of the engagement, including the size or complexity of the business.

6. *Independence, Integrity, and Objectivity.* The engagement quality reviewer must be independent of the company, perform the engagement quality review with integrity, and maintain objectivity in performing the review. Assistants also must be independent, perform the assigned procedures with integrity, and maintain objectivity in performing the review.

~~Note: The reviewer may use assistants in performing the engagement quality review. Personnel assisting the engagement quality reviewer also must be independent, perform the assigned procedures with integrity, and maintain objectivity in performing the review.~~

7. To maintain objectivity, the engagement quality reviewer should not: (a) make decisions on behalf of the engagement team; (b) assume any of the responsibilities of the engagement team; or (c) supervise the engagement team with respect to performance of the engagement subject to the engagement quality review. The person who has overall responsibility for the engagement remains responsible for the engagement and its performance, notwithstanding the involvement of the engagement quality reviewer.

8. The engagement quality reviewer may not be the person who had overall responsibility for either of the two audits preceding the audit subject to the engagement quality review.

Engagement Quality Review for an Audit

9. *Engagement Quality Review Process.* In an audit engagement, the engagement quality reviewer should ~~evaluate~~review the significant judgments made by the engagement team and the related significant conclusions reached in forming the overall conclusion on the engagement and in preparing the engagement report. To identify and ~~evaluate~~review the significant judgments and related significant conclusions, the engagement quality reviewer

² ~~PCAOB interim quality control standards describe the competencies required of a person who has the overall responsibility for an engagement (or any practitioner in charge of an attest engagement). See QC sec. 40, *The Personnel Management Element of a Firm's System of Quality Control—Competencies Required by a Practitioner in Charge of an Attest Engagement.*~~

should perform the procedures described in paragraph 10 by holding discussions with the person with overall responsibility for the engagement, by holding discussions with other members of the engagement team as necessary, and by reviewing selected documentation as considered appropriate by the engagement quality reviewer.

10. In an audit, reviewing the significant judgments and related significant conclusions referenced in paragraph 9, the engagement quality reviewer should, as he or she deems appropriate, may:

- a. EvaluateReview significant judgments made by the engagement team and the related significant conclusions reached pertaining to engagement planning, including –
 - The consideration of the firm's recent engagement experience with the company ~~and risks identified in connection with the firm's client acceptance and retention process,~~
 - The consideration of the company's business, recent significant activities, and related financial reporting issues and risks, and
 - The judgments made about materiality and the effect of those judgments on ~~the engagement strategy~~planning.
- b. Evaluate theReview significant judgments made by the engagement team and the related significant conclusions reached pertaining to risk assessments and audit responses, including the identification of significant risks, including risk of material fraud risks, and the engagement procedures performed in response to significant risks.
- c. Review the engagement team's evaluation of the firm's independence in relation to the engagement by considering written communications that the engagement team had with the client (in accordance with PCAOB Rule 3526) and other relevant issues that come to the attention of the engagement quality reviewer in performing the procedures specified under this paragraph.
- d. EvaluateConsider significant judgments made by the engagement team and the related significant conclusions reached about (1) the materiality and disposition of corrected and uncorrected identified misstatements and (2) the severity and disposition of identified control significant deficiencies and material weaknesses.
- e. Determine ifConsider whether appropriate matters have been communicated, or identified for communication to the audit committee, management, and other parties, such as regulatory bodies.
- f. Determine ifConsider whether appropriate consultations have taken place ~~on difficult or contentious matters.~~ Review the documentation with respect

to significant judgments, including conclusions, and documentation of such consultations.

- g. Read the financial statements, management's report on internal control, and the related engagement report.
- h. Read other information in documents containing the financial statements to be filed with the Securities and Exchange Commission ("SEC")³² and ~~evaluate~~consider whether the engagement team has taken appropriate action with respect to any material inconsistencies with the financial statements or material misstatements of fact of which the engagement quality reviewer is aware.
- i. Review the engagement completion document⁴³ and confirm with the person who has overall responsibility for the engagement that there are no significant unresolved matters.

11. ~~*Evaluate*~~Consider *Engagement Documentation*. In an audit, the engagement quality reviewer should ~~evaluate~~consider whether the engagement documentation that he or she reviewed when performing the procedures ~~required by paragraph 10~~in accordance with this standard –

- a. Indicates that the engagement team responded appropriately to significant risks, and
- b. Supports the conclusions reached by the engagement team with respect to the matters reviewed.

~~12. *Concurring Approval of Issuance*. In an audit, the engagement quality reviewer may provide concurring approval of issuance only if, after performing with due professional care⁵ the review required by this standard, he or she is not aware of a significant engagement deficiency.~~

12. Note: A significant engagement deficiency in an audit exists when*Concurring Approval of Issuance*. In an audit, the engagement quality reviewer may not provide concurring approval of issuance if, after performing the review required by this standard, he or she is aware that (1) the engagement team failed to obtain sufficient appropriate evidence in accordance with the standards of the PCAOB, (2) the engagement team reached an inappropriate overall

³² See paragraphs .04-.06 of AU sec. 550, *Other Information in Documents Containing Audited Financial Statements*; AU sec. 711, *Filings Under Federal Securities Statutes*.

⁴³ PCAOB Auditing Standard No. 3, *Audit Documentation*, requires the auditor to identify all significant findings or issues in an engagement completion document.

~~⁵ See AU sec. 230, *Due Professional Care in the Performance of Work*.~~

conclusion on the subject matter of the engagement, or (3) the engagement report is not appropriate in the circumstances, ~~or (4) the firm is not independent of its client.~~

13. In an audit, the firm may grant permission to the client to use the engagement report only after the engagement quality reviewer provides concurring approval of issuance.⁶⁴

Engagement Quality Review for a Review of Interim Financial Information

14. *Engagement Quality Review Process.* In an engagement to review interim financial information, the engagement quality reviewer should ~~evaluate~~review the significant judgments made by the engagement team and ~~the~~any related significant conclusions reached in forming the overall conclusion on the engagement and in preparing the engagement report, if a report is to be issued. To identify and ~~evaluate~~review the significant judgments and any related significant conclusions, the engagement quality reviewer should perform the procedures described in paragraph 15 by holding discussions with the person with overall responsibility for the engagement, by holding discussions with other members of the engagement team as necessary, and by reviewing selected documentation as considered appropriate by the engagement quality reviewer.

15. ~~In a review of interim financial information, reviewing the significant judgments and any related significant conclusions referenced in paragraph 14, the engagement quality reviewer should, as he or she deems appropriate, may:~~

- a. ~~Evaluate~~Review significant judgments made by the engagement team and any related significant conclusions reached pertaining to engagement planning, as performed in accordance with AU sec. 722.11-13, including the consideration of –
 - ~~The firm's recent engagement experience with the company and risks identified in connection with the firm's client acceptance and retention process,~~company's business and its internal control, and
 - ~~The company's business, recent significant activities, and related financial reporting issues and risks, and~~
 - ~~The nature of identified risks of material misstatement due to fraud.~~

⁶⁴ Concurring approval of issuance by the engagement quality reviewer also is required when reissuance of an engagement report requires the auditor to update his or her procedures for subsequent events. In that case, the engagement quality reviewer should update the engagement quality review by addressing those matters related to the subsequent events procedures.

= The engagement team's identification of events, transactions, or assertions to which inquiries may be directed or analytical procedures applied.

- b. Perform the procedures described in paragraphs 10.c through 10.f., with the exception of 10.d.(2).
- c. Read the interim financial information for all periods presented ~~and for the immediately preceding interim period~~, management's disclosure for the period under review, if any, about changes in internal control over financial reporting, and the related engagement report, if a report is to be ~~filed with the SEC~~issued.
- d. Read other information in documents containing interim financial information to be filed with the SEC⁷⁵ and ~~evaluate~~consider whether the engagement team has taken appropriate action with respect to material inconsistencies with the interim financial information or material misstatements of fact of which the engagement quality reviewer is aware.
- e. Review the engagement completion document and confirm with the person who has overall responsibility for the engagement that there are no significant unresolved matters.

16. ~~*Evaluate*~~*Consider* *Engagement Documentation.* In a review of interim financial information, the engagement quality reviewer should ~~evaluate~~consider whether the engagement documentation that he or she reviewed when performing the procedures ~~required by paragraph 15~~in accordance with this standard supports the review performed by the engagement team.

- a. ~~Indicates that the engagement team responded appropriately to significant risks, and~~
- b. ~~Supports the conclusions reached by the engagement team with respect to the matters reviewed.~~

~~17. *Concurring Approval of Issuance.* In a review of interim financial information, the engagement quality reviewer may provide concurring approval of issuance only if, after performing with due professional care the review required by this standard, he or she is not aware of a significant engagement deficiency.~~

17. Note: A significant engagement deficiency in a review of interim financial information exists when*Concurring Approval.* In a review of interim financial information, the engagement quality reviewer may not provide concurring approval if, after performing the

⁷⁵ See paragraph .18f of AU sec. 722, *Interim Financial Information*; AU sec. 711, *Filings Under Federal Securities Statutes*.

review required by this standard, he or she is aware that (1) the engagement team failed to perform interim review procedures necessary in the circumstances of the engagement, (2) the engagement team reached an inappropriate overall conclusion on the subject matter of the engagement, or (3) the engagement report, if a report is to be issued, is not appropriate in the circumstances, or (4) ~~the firm is not independent of its client.~~

18. In a review of interim financial information, the firm may grant permission to the client to use the engagement report (or communicate an engagement conclusion to its client, if no report is issued) only after the engagement quality reviewer provides concurring approval ~~of issuance.~~

Documentation of an Engagement Quality Review

19. ~~Documentation of~~ if an engagement quality review approval under paragraph 12 or 17 is provided, documentation of the review should be included in the engagement documentation and should contain sufficient information to identify:

- a. The engagement quality reviewer and others who assisted the reviewer,
- b. ~~The documents~~ As considered appropriate by the engagement quality reviewer, the documents relating to the significant judgments made by the engagement team and related significant conclusions reached that were reviewed by the engagement quality reviewer and others who assisted the reviewer,
- c. ~~The significant discussions held by the engagement quality reviewer and others who assisted the reviewer, including the date of each discussion, the specific matters discussed, the substance of the discussion, and the participants, and~~ procedures performed in accordance with this standard, and
- d. The date the engagement quality reviewer provided concurring approval of issuance ~~or, if no concurring approval of issuance was provided, the reasons for not providing the approval.~~

20. The requirements related to retention of and subsequent changes to audit documentation in AS No. 3 apply with respect to the documentation of the engagement quality review.



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Date: April 20, 2009

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

Re: PCAOB Rulemaking Docket Matter No. 025

Dear Board:

We are pleased to comment on the Public Company Accounting Oversight Board's (PCAOB) *Proposed Auditing Standard – Engagement Quality Review* (the Proposed Standard). Eli Lilly and Company reviewed PCAOB Rulemaking Docket Matter No. 025, the Proposed Standard reissued for comment on March 4, 2009.

We generally agree with the changes made since the original proposed auditing standard was released in 2008. We are writing this letter to provide further comments on the views discussed and consider when finalizing this Proposed Standard as we have some additional concerns for you to address.

Issue 1: Objective of Engagement Quality Review

We fully support an independent review to reach appropriate conclusions on areas of significant judgment. The objective defined in paragraph 2 of the Proposed Standard sets the appropriate focus. We want to ensure the audit firms do not confuse the Engagement Quality Review with their internal Audit Quality Review, which is much more detailed and whose objective is to ensure the engagement team has complied with all policies and procedures established by the audit firm. Any confusion using this common terminology of “Quality Review” would only result in unnecessary additional work and higher audit fees.

Issue 2: Documentation requirements for the Quality Review

We believe that an effective Quality Review can be performed by holding discussions with the engagement team and by reviewing existing audit and interim documentation. By clearly stating in paragraphs 9 and 14, the Quality Reviewer should use existing audit and interim documentation, as applicable, it will prevent a reaudit of the engagement.

Issue 3: Audit Inspections Expectations for Documentation of Engagement Quality Review

We believe the key to an effective implementation of the Proposed Standard includes specific guidance provided for the PCAOB audit inspections to search for an effective and efficient Quality Review. The PCAOB audit inspections should provide feedback to the audit firms if the documentation goes beyond what is necessary to support an effective Engagement Quality Review. Over auditing and excessive documentation of the Quality Reviews will only result in higher audit fees, which are not the intent of the Proposed Standard, but rather a higher quality of the audit and interim engagements.

We appreciate your consideration of our views and concerns regarding the Proposed Standard. If you have any questions, or would like to discuss our comments further, please call me at (317) 276-2024.

Sincerely,

ELI LILLY AND COMPANY

S/Arnold C. Hanish
Vice President and
Chief Accounting Officer

Mr. J. Gordon Seymour
Secretary
Public Company Accounting Oversight Board
1666 K Street, N.W.
Washington, D.C. 20006-2803

14 April 2009

Proposed Auditing Standard - Engagement Quality Review; PCAOB Rulemaking Docket Matter No. 025

Dear Mr. Seymour:

We are pleased to comment on the Public Company Accounting Oversight Board's ("PCAOB" or the "Board") Proposed Auditing Standard - Engagement Quality Review ("the Proposed Standard").

We support the Board's efforts to adopt a comprehensive standard consistent with Section 103 (a) (2) (A) (ii) of the Sarbanes-Oxley Act, which requires that the Board adopt a standard that registered public accounting firms "provide a concurring or second partner review and approval of [each] audit report (and other related information), and concurring approval in its issuance, by a qualified person (as prescribed by the Board) associated with the public accounting firm, other than the person in charge of the audit, or by an independent reviewer (as prescribed by the Board)."

We believe that an engagement quality review that focuses on significant judgments made and related conclusions reached by the engagement team is effective in promoting audit quality. We also are of the view that engagement quality reviews are but one element of an overall system of quality control and proposed changes to the Board's interim standards should be considered in the context of a firm's system of quality control taken as a whole.

We commend the Board for the modifications and clarifications made to the Proposed Standard. We believe that the Proposed Standard more appropriately defines the requirements of the engagement quality review and adequately addresses many of the comments made by us and others on the original proposal. However, we believe that additional modifications would provide further clarity regarding the documentation of an engagement quality review, the concurring approval of issuance, the required competence of the engagement quality reviewer and the effective date of the final standard. Our comments about these and other matters are provided below.

Paragraph 19 - Documentation of an Engagement Quality Review

Paragraph 19(c) requires that documentation of the engagement quality review include sufficient documentation of the significant discussions held by the engagement quality reviewer and others who assisted the reviewer, including the date of each discussion, the specific matters discussed, the

substance of the discussion, and the participants. We believe the requirement is unnecessary and unduly burdensome, and we recommend it be deleted.

PCAOB Auditing Standard No. 3, *Audit Documentation*, states that “audit documentation...provides the reviewer with written documentation of the evidence supporting the auditor’s significant conclusions.” Separate documentation of significant discussions involving the engagement quality reviewer throughout the course of the audit and related interim reviews will duplicate other documentation already required to be included in the audit workpapers that provide evidence supporting significant audit conclusions. Additionally, significant discussions held by the engagement quality reviewer throughout the course of the audit and interim reviews may reflect fact patterns or matters that are no longer relevant to the engagement team’s conclusions and therefore would no longer be relevant audit documentation. We also believe it is unreasonable to expect the engagement quality reviewer to know, at the time of the discussions, whether such discussions will in fact be significant and therefore whether documentation of such discussions will be necessary to demonstrate compliance with the Proposed Standard. Some auditors may therefore determine that it would be necessary to document each discussion, which would be overly burdensome and costly and could possibly inhibit discussions or collaboration with the engagement quality reviewer. We do not believe this was the Board’s intent.

The Board indicates on page 24 of its Release accompanying the Proposed Standard (“Release”) that it has observed deficiencies in the documentation of concurring partner reviews based on information and findings from inspection teams, enforcement cases and academic research that may have contributed to the failure to properly address the concurring partner’s findings. It is our experience that matters considered and resolved through discussions with the engagement quality reviewer that are determined to be important accounting and auditing matters are documented in the engagement completion document. The documentation of such matters and their resolution would therefore be subject to review by the engagement quality reviewer as required by paragraph 10(i) of the Proposed Standard. We believe these procedures combined with the requirement of paragraph 19(b) to identify the documents reviewed by the engagement quality reviewer will result in sufficient documentation of the significant matters that the engagement quality reviewer focused on when performing the engagement quality review and enable the Board’s inspectors to evaluate whether the engagement quality review was appropriately performed.

Paragraphs 12 and 17 - Concurring Approval of Issuance

The Proposed Standard indicates that the engagement quality reviewer may provide concurring approval of issuance only if, after performing with due professional care the review required by the standard, he or she is not aware of a significant engagement deficiency. We commend the Board for requiring that the engagement quality review be conducted with due professional care, which we believe is preferable to the “knows or should know” standard provided in the original proposal. We believe these revisions convey appropriate standards of performance and care that are consistent with the objectives and requirements of the Proposed Standard. We agree with the Board’s observation that due professional care is a concept familiar to auditors and consistent with other auditing standards.

However, we respectfully disagree with the Board's statement on page 24 of the Release that the requirement to exercise due professional care imposes on a reviewer essentially the same requirement as the condition stated in the Board's original proposal (i.e., "knows or should know"). We continue to believe the condition "knows or should know" would be interpreted as imposing significant additional obligations on the engagement quality reviewer and therefore would elicit a level of effort that is not consistent with the objectives and requirements of the Proposed Standard. We recommend removing such language from the release that accompanies the final Engagement Quality Review standard.

Paragraph 5 - Qualifications of an Engagement Quality Reviewer-Competence

We recommend that, when describing the competencies that the engagement quality reviewer must possess, the Board refer to those competencies required to serve as the engagement quality reviewer, rather than to the competencies required to serve as the engagement partner. This description would be consistent with International Standards on Quality Control (ISQC) 1 (R), paragraph 39. We are concerned that the Proposed Standard could be interpreted as requiring the engagement quality reviewer to possess all of the same competencies as the engagement partner. We believe the engagement quality reviewer can possess sufficient competence to perform the engagement quality review without possessing all of the same competencies of the engagement partner.

What constitutes sufficient and appropriate technical expertise, experience and authority depends on the circumstances of the engagement and the personnel assigned to the engagement. Therefore, many judgments are made when making assignments of the engagement quality reviewer and firms need a certain level of flexibility when making these decisions. Defining the competencies from the engagement quality reviewer perspective and removing the language of "the same type of engagement" from the Proposed Standard will broaden the criteria for assigning the engagement quality reviewer, while still providing the necessary framework for determining that an appropriate individual is selected.

Effective Date of the Standard

We believe that the effective date of the final Engagement Quality Review standard should coincide with the beginning of the audit engagement period to allow for the requirements to be applied to interim reviews and audits in the same fiscal year. Linking the effective date to the beginning of the audit cycle will allow the engagement quality reviewer to comply with the requirements during audit planning activities and timely reviews of interim financial information. Accordingly, we recommend that the effective date of the final standard be for audits of fiscal years beginning on or after December 15, 2009 and for interim reviews within such fiscal years.

Other Aspects of the Proposed Standard

Paragraph 2 - Objective

We commend the Board for including an objective of the engagement quality review in the Proposed Standard. The objective allows regulators, investors, audit committees and company management to

have a consistent understanding of the purpose of the engagement quality review. It allows auditors to apply professional judgment in determining the nature and extent of the review procedures to be performed to meet the requirements of the Proposed Standard. It also aids in differentiating the role and function of the engagement quality reviewer from that of the engagement partner and other members of the engagement team.

Paragraphs 3-8 - Qualifications of an Engagement Quality Reviewer

Paragraph 4 of the Proposed Standard states that an engagement quality reviewer must have competence, independence, integrity and objectivity. In order to clarify what is meant by this requirement, we believe the Proposed Standard should reference the PCAOB interim quality control standards that fully describe these requirements (QC sec. 20, *System of Quality Control for a CPA Firm's Accounting and Auditing Practice*).

We commend the Board for the revisions made to the Proposed Standard regarding the objectivity of the engagement quality reviewer. We believe that the revised requirements allow for ongoing consultations between the engagement team and the engagement quality reviewer, which we believe are critical to the audit process.

Also with respect to the objectivity of the engagement quality reviewer, we commend the Board for expanding the phrase "supervise the engagement team with respect to the engagement subject to the engagement quality review." However, we do not believe this is sufficiently clear to denote that partners in a leadership position in a firm, region, service line, or industry practice are permitted to perform engagement quality reviews. We recommend that the final standard more explicitly state the Board's intention to not prohibit such persons from performing engagement quality reviews if otherwise qualified.

Paragraph 10 - Engagement Quality Review for an Audit

Paragraphs 10(e) and 10(f) require the engagement quality reviewer to "determine if appropriate matters have been communicated, or identified for communication" and "determine if appropriate consultations have taken place on difficult or contentious matters." We believe these requirements could be interpreted to go beyond the other requirements of the Proposed Standard that are focused on the evaluation of the work performed by the engagement team. Therefore, we believe the procedures in paragraphs 10(e) and 10(f) of the Proposed Standard should be modified to indicate that the engagement quality reviewer should make an evaluation of the appropriateness of the matters described in paragraphs 10(e) and 10(f) based upon performing all of the other procedures set forth in paragraph 10.

We also suggest that the Board modify paragraphs 10(a), 10(b) and 10(d) to indicate that the engagement quality reviewer should "review" (rather than "evaluate") the applicable items to make clear that these procedures are intended to apply to significant judgments made by the engagement team. This change is consistent with the direction provided in paragraph 9 and will add appropriate clarity to the requirements.

Further, we believe paragraph 10(b) is not sufficiently clear to describe the extent of procedures required of the engagement quality reviewer with regard to risk assessments and audit responses. We believe a partner performing an engagement quality review could interpret the phrase, "evaluate the risk assessments and audit responses," to mean that he or she should review the audit responses for all areas of the audit. We believe such an interpretation would result in performing unnecessary procedures and also would appear to conflict with the phrase appearing later in paragraph 10(b) indicating the engagement quality reviewer should evaluate "the engagement procedures performed in response to significant risks." We also observe that paragraph 11(a) requires the engagement quality reviewer to evaluate whether the engagement documentation reviewed "indicates that the engagement team responded appropriately to significant risks." We recommend that the Board modify paragraph 10(b) to clarify that the engagement quality reviewer should evaluate the audit responses to significant risks.

Paragraphs 14-18 - Engagement Quality Review for a Review of Interim Financial Information

Paragraph 15(c) of the Proposed Standard indicates the engagement quality reviewer should read the related engagement report, if a report is to be filed with the SEC. We believe that the engagement quality reviewer should read the related engagement report, if a report is to be issued, regardless of whether the report is filed with the SEC.

Paragraph 17 of the Proposed Standard requires the engagement quality reviewer to provide concurring approval of issuance. However, as engagement reports are not issued in every review of interim financial information, the final standard should refer to the engagement quality reviewer's "concurring approval" rather than "concurring approval of issuance."

Relationship with Quality Control Standards

The note to paragraph 4 of the Proposed Standard indicates the firm's quality control policies and procedures should include provisions to provide the firm reasonable assurance that an engagement quality reviewer has sufficient competence, independence and integrity to perform the engagement quality review. While we agree with this statement, we do not believe that such a statement should be included in auditing standards, but instead should be included in quality control standards.

Having a system of internal quality control policies and procedures that, among other things, specify the criteria and procedures for the assignment of the firm's personnel to engagements is a firm requirement. Audit personnel, including the engagement quality reviewer, are required to follow auditing standards in the preparation and issuance of audit reports. We believe that delineating the audit firm's requirements in the quality control standards and the auditor's requirements in the auditing standards and the attestation standards, as appropriate, lends clarity to the requirements in the standards.



* * * *

We would be pleased to discuss our comments with members of the Public Company Accounting Oversight Board or its staff.

Sincerely,

Ernst + Young LLP



April 20, 2009

Office of the Secretary
PCAOB
1666 K Street, N.W.
Washington, D.C. 20006-2803

Re: PCAOB Rulemaking Docket Matter No. 025

Dear Board:

The Committee on Corporate Reporting (“CCR”) of Financial Executives International (“FEI”) wishes to share its views on the Public Company Accounting Oversight Board’s (“PCAOB”) Proposed Auditing Standard—Engagement Quality Review (“proposed standard”). FEI is a leading international organization of senior financial executives. CCR is the senior technical committee of FEI, which reviews and responds to research studies, statements, pronouncements, pending legislation, proposals and other documents issued by domestic and international agencies and organizations. This document represents the views of CCR and not necessarily the views of FEI or its members individually.

We support the Board’s efforts to adopt a comprehensive standard consistent with Section 103(a)(2)(A)(ii) of the Sarbanes-Oxley Act. We agree that the engagement quality review (“EQR”) is an opportunity for the auditor to discover any significant engagement deficiencies before issuing its opinion, and that a well-performed EQR can be an effective safeguard against erroneous or insufficiently supported audit opinions. Accordingly, an effective EQR can contribute to audit quality and reduce the need for restatements.

We commend the Board on the revised standard that has been proposed. Overall, we believe the proposed standard is better articulated, in a less prescriptive tone, than the Board’s original proposed standard. We expect that the revised proposed standard will better drive the audit behavior that the Board expects.

However, we do have the following suggestions that we believe the Board should consider in preparing the final standard:

- 1) We agree with the Board’s clarification that the engagement quality review be performed with “due professional care” as opposed to the language in the original proposal which established that a reviewer could not provide concurring approval of issuance if he or she “knows, or should know based upon the requirements of

the standard” of deficiencies in the work performed or conclusions reached in the engagement. However, we are concerned that language in the Board’s Release that accompanies the proposed standard could be misinterpreted by certain constituents as contradicting the “due professional care” requirement contained in the actual proposed standard. Specifically the comment on p. 24 of the Board’s Release reads’ “. . . *the requirement to exercise due professional care imposes on a reviewer essentially the same requirement as the ‘knows or should know based on the requirement of this standard’ formulation in the Board’s original proposal.* We believe the “due professional care” language should be used exclusively throughout the entire document as it clearly and effectively establishes the standard against which an EQR should be both performed and measured.

2) We also believe that Paragraph 19, regarding documentation of the EQR, should be revised. Specifically, we believe that the provisions of 19c, as currently articulated, are too prescriptive and would drive an excessive amount of documentation that is not necessary to further the objective of well-performed EQRs in quality audits. We suggest the following modifications to Paragraph 19c as one way to improve this provision:

“The ~~significant~~ discussions held by the engagement quality reviewer and others who assisted the reviewer that were important to determine whether to provide concurring approval of issuance, including the date of each discussion, the specific matters discussed, and the substance of the discussions, and the participants, if not otherwise evident in the audit documentation of significant findings or issues^{fn} reviewed by the engagement quality reviewer and”

^{fn} See Auditing Standard No. 3, paragraph 12, regarding audit documentation of significant findings or issues.

We appreciate the PCAOB’s consideration of these matters and welcome the opportunity to discuss any questions you have with respect to our comments.

Sincerely,



Arnold C. Hanish
Chairman, Committee on Corporate Reporting
Financial Executives International



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April 17, 2009

Public Company Accounting Oversight Board
Attention: Office of the Secretary
1666 K Street, N.W.
Washington, D.C. 20006-2803

RE: Rulemaking Docket Matter No. 025
Proposed Auditing Standard – Engagement Quality Review

Members of the Board,

I appreciate the opportunity to submit my comments to the Board with respect to the proposed auditing standard on engagement quality review. I retired from public accounting in 2007 after 27 years at Deloitte & Touche LLP and am currently a full-time faculty member at the University of Notre Dame teaching undergraduate and graduate courses in accounting and auditing.

My comments are as follows:

1. Should the standard require an EQR for other kinds of engagements performed according to PCAOB standards? If so, what types of engagements should be included and what should an EQR of such engagements entail?

The PCAOB's oversight responsibilities extend to all engagements related to filings with the Securities and Exchange Commission. Accordingly, I believe that EQR should be required for all filings in which the auditors' opinion/review report is included or incorporated by reference. The applicability of PCAOB standards to an engagement commences with the first filing of a company's financial statements in an initial public offering. The potential for impact on the broader public commences with an IPO and the audit of the financial statements included in such document should be of the same quality as that for all other public companies. Accordingly, EQR should be required in connection with those and all other registrations of securities and should include engagements to provide a letter to underwriters.

Finally, EQR should be required of all communications related to the audit or review engagement including communications with those charged with governance. The engagement quality reviewer will have the base of knowledge necessary to help insure such communications are comprehensive.

2. Is the objective in the re-proposed standard appropriately formulated? Does it articulate the purpose of an EQR?

I believe the objective is appropriately stated.

3. Will this objective contribute to a more thoughtful and effective EQR?

The objective states what an EQR should be and what I believe an EQR has been, when properly performed. The objective will not contribute to a more thoughtful and effective EQR; however, the standard as a whole likely will.

4. Is it appropriate to explicitly require a reviewer from within the firm to be a partner or an individual in an equivalent position?

I believe it is absolutely appropriate for an engagement quality reviewer to be a partner or equivalent.

5. Should the standard allow qualified accountants who are not employed by an accounting firm to conduct the review?

As an accommodation for smaller firms who do not have sufficient numbers of partners, I believe it is appropriate. However, I believe it should be restricted to those situations where personnel constraints make it necessary. The routine “out-sourcing” of EQR as a means to enhance engagement profitability should not be encouraged.

The Board should consider requiring the engagement quality reviewer be licensed as a CPA. The discussion in the release referred to the possibility that those outside the firm who are qualified to perform such reviews might be, for example, retired partners or professors of accounting. While it may seem implicit in PCAOB Interim Quality Control Standards (QC 40), the discussion in that standard is not specific as to what actually constitutes competency to function as the practitioner in charge of the audit of a public company. Holding a current, active license would help insure that the engagement quality reviewer has maintained some minimal level of continuing professional education that is relevant to the current practice of public accounting and conduct of audits.

6. Should the standard prohibit the engagement partner from serving as the reviewer for a period of time following his or her last year as the engagement partner? If so, is two years sufficient, or should it be extended?

I agree a two year restriction is appropriate, however I do not believe it should be restricted to the partner responsible for the engagement. Many larger engagements have multiple partners involved who should be considered for this restriction. Additionally, a new partner who would not have been subject to rotation requirements as a manager could have spent a number of years serving the registrant prior to becoming a partner and should not be placed in the position of functioning as the engagement quality reviewer for his former client and former engagement supervisor. All professional personnel should have a two year restriction prior to being assigned as the engagement quality reviewer. If the Board does not believe there are risks related to this area for these other personnel, then I question the rationale for the restriction related to the lead engagement partner.

7. Are the descriptions of the scope and extent of EQR procedures contained in the re-proposed standard appropriate? Will the performance of these procedures result in a high-quality EQR? If not, how should these procedures be revised?

The procedures as stated are appropriate. However, the Board should consider adding a statement to the effect that the engagement quality reviewer be given access to any and all documentation and engagement personnel he or she believes necessary to accomplish an effective review. This could become a source of contention in those situations where the engagement quality reviewer is from outside the firm. Neither the engagement partner nor the engagement partner’s firm should have the ability to limit the scope of the EQR.

8. Are the specifically required procedures appropriately tailored to reflect the difference in scope between an audit and an interim review?

They are; however I suggest the Board consider an additional requirement that the engagement quality reviewer consider the need to review selected working papers from the preceding annual audit (if this is a recurring engagement) such as the engagement completion document, summary of corrected and uncorrected misstatements, and any other materials the engagement quality reviewer believes is necessary to establish or regain familiarity with the client and so perform an effective EQR of the interim information. This is important for a newly assigned engagement quality reviewer and may be particularly important for a reviewer from outside of the firm as discussed in my comments to the preceding question.

9. Do the specifically required procedures sufficiently focus the reviewer on areas of highest risk? Are there other procedures that should be required?

I believe the procedures focus on areas of risk, but again the language should not be such as to suggest a limitation on what engagement quality reviewers can do should they conclude that additional procedures are necessary.

10. Is the standard for the engagement quality reviewer's concurring approval of issuance appropriately described in the re-proposed standard? Is the first condition appropriately tailored to reflect the difference in scope between an audit and an interim review?

I believe the standard is appropriate; no report should be issued without the concurrence of the engagement quality reviewer. I believe the first condition would provide me with sufficient guidance were I functioning as an engagement quality reviewer.

11. Are the documentation requirements in the re-proposed standard appropriate? If not, how should they be changed?

I believe the requirements are appropriate. They give the engagement quality reviewer sufficient leeway to determine how best to document the completion of the review. It permits development by the firms of standardized checklists, templates for memoranda, electronic completion documents or some combination of these and accordingly is not burdensome.

Finally, as I stated in my comment letter on the earlier version of this standard, I believe that the engagement quality review process is a "second line of defense" in the area of engagement quality. Accordingly, I encourage the Board to consider a project to address the qualifications and duties of the members of the engagement team – the "first line of defense" – with respect to engagement conduct and quality.

I appreciate the opportunity to offer my comments.

Sincerely,

s/ James L. Fuehrmeyer, Jr.

James L. Fuehrmeyer, Jr. MBA, CPA
Associate Professional Specialist
Department of Accountancy
University of Notre Dame
Notre Dame, IN 46556-5646



April 20, 2009

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Re: PCAOB Rulemaking Docket Matter No. 025, *Proposed Auditing Standard – Engagement Quality Review*

Dear Board Members and Staff:

We appreciate the opportunity to comment on the proposed auditing standard, *Engagement Quality Review*. We support the Public Company Accounting Oversight Board's ("Board" or "PCAOB") mission to develop auditing standards that promote audit quality, and we believe that a robust and effective engagement quality review enhances audit quality. In our opinion, an objective engagement quality review that focuses on a review of significant matters, including significant judgments made and conclusions reached by the engagement team, will accomplish that purpose.

We understand that the PCAOB received many comment letters on the first proposed Engagement Quality Review standards. We observe that many of those comments have informed the re-proposed standard, and we appreciate the PCAOB's careful and thoughtful consideration of those comments. Although we have some additional thoughts for your consideration, we believe that the re-proposed standard improves on the first proposal in advancing the quality of audits, increasing confidence in the capital markets, and setting appropriate expectations as to what an engagement quality review is or is not.

We would like to take the opportunity to offer to work with the PCAOB in the future, not only during the formal consultation phase of a project, but throughout the project. We recognize that high-quality standards that are in the public interest are also in the long-run interest of the profession, but standards that set unrealistic expectations are not in anybody's interest. Input from the firms would result in high-quality standards, and enable the PCAOB to expedite its standards setting activities, which we believe would be in the best interests of the PCAOB, the firms and most importantly, the public.

Objective of the engagement

We strongly support the inclusion of the objective in the proposed standard. We believe that the objective will enable the engagement quality reviewer to know when he or she has fulfilled

the objective of the standard. The objective will also help define who would be qualified to perform an engagement quality review in that the person qualified to perform the review would need to have the skills to meet the objective. The objective also will clarify expectations of third parties, for example, financial statement users and regulators, with respect to what an engagement quality review is and is not.

We suggest the following edits to the objective in paragraph 2, and similar edits to paragraph 9, to clarify that (1) the engagement quality reviewer meets the objective based on the results of the procedures required by the standard, and (2) the conclusions that should be the focus of the engagement quality review are those that result from the significant judgments.

The objective of the engagement quality reviewer is to perform an evaluation, based on the results of the procedures required by this standard, of the significant judgments made by the engagement team and the related conclusions reached in forming the overall conclusion on the engagement and in preparing the engagement report, if a report is to be issued, in order to determine whether to provide concurring approval of issuance.

The engagement quality review process

We believe that the current proposal much better describes the engagement quality review process than did the first proposal by:

- adopting a “negative assurance” standard as opposed to a “positive assurance” standard;
- relying on the concepts of due professional care, rather than imposing a “knows or should know” standard; and
- acknowledging that the engagement quality reviewer performs the engagement quality review through discussions with the engagement team and the review of documentation.

We believe that an engagement quality reviewer who performs the review in accordance with this proposed standard, using appropriate professional judgment, and due professional care as described in the Board’s Interim Standards in AU 230, *Due Professional Care in the Performance of Work*, would have an adequate basis to determine if he or she could provide concurring approval of issuance. This new construction helps prevent the unintended consequence of engagement quality reviewers spending inordinate amounts of time searching for, and coming to a positive conclusion about what they “should know.” At the same time, the requirement to perform the engagement with due professional care does not allow the engagement quality reviewer to turn a blind eye to conditions that should prohibit him or her from providing concurring approval of issuance.

We agree with the formulation of the requirement in paragraph 12 of the proposed standard; however, we believe the Board has introduced an inappropriate inconsistency as well as confusion in the release by stating that, “the requirement to exercise due professional care imposes on a reviewer essentially the same requirement as the ‘knows, or should know based on the requirements of this standard’ formulation in the Board’s original proposal.” We do not, in fact, believe this is a true statement. We also believe the courts have held these to be two

different standards. We do not think it appropriate for the Board to set a requirement in the standard, and then make a statement in the release that the words really mean something other than what they say. If the Board chooses not to change the release then it has, apparently, retained the “knows or should know” requirement. This, in turn, likely will lead engagement quality reviewers to obtain a level of knowledge comparable to that of engagement partners in order to avoid potential consequences of the inspection process.

We appreciate that paragraph 9 of the proposal states that the procedures described in paragraph 10 are to be performed by holding discussions with the engagement team and reviewing documentation. However, as worded, we do not believe that the requirements in 10(e) and 10(f) could be accomplished through discussions with the engagement team and reviewing documentation. These requirements to *determine* if appropriate matters have been communicated and to *determine* if appropriate consultations have taken place would require the engagement quality reviewer to identify matters that were *not* communicated or subject to consultation, but maybe should have been. To accomplish this requirement, the engagement quality reviewer would have to go beyond discussions with the engagement team and reviewing the documentation. There is no limit to how far the engagement quality reviewer would have to search for those items that had not been recognized by the engagement team as requiring communication or consultation. We suggest that the requirement be specifically limited to evaluating whether matters identified in the workpapers, or through discussions with the engagement team, have been communicated or were subject to appropriate consultation.

With respect to the evaluation of engagement documentation, we support the Board’s decisions to:

- Replace the phrase “documentation of the matters that were subject to the engagement quality review procedures” with “documentation that he or she reviewed when performing the procedures”;
- Require the reviewer to evaluate whether such documentation supports “conclusions reached by the engagement team with respect to the matters reviewed” but not also “the conclusions and representations in the engagement report”; and
- Remove the requirement for the reviewer to evaluate the documentation for consistency with AS No. 3.

Engagements for which an engagement quality review is required

We continue to support the PCAOB’s proposal to require that all registered public accounting firms – not just those that were members of the American Institute of Certified Public Accountant’s SEC Practice Section in April 2003 – be required to comply with the final standard. We believe that this certainly is in the public interest, and is consistent with the requirements of the Sarbanes-Oxley Act of 2002.

We agree with the Board’s decision to customize the engagement quality review requirements for audits and interim reviews to reflect the differences in scope between these engagements. We found the approach of specific requirements for audits and interim reviews in two separate

sections to be very helpful. We believe that this should better align the engagement quality review with the engagement under review, and clarify which requirements apply to which engagements.

We further support the Board's decision to limit the applicability of these requirements to engagement quality reviews of audits and interim reviews of financial statements. We believe this allows the Board to maintain the specificity in this proposed standard, and has the added benefit of keeping the auditing standards and the attestation standards clearly delineated. Should the Board believe engagement quality reviews are desirable for attestation engagements, those requirements should be provided for in the attestation standards rather than in the auditing standards.

We believe it is inappropriate for requirements of the firm to be included in the auditing standards, as is done in the note to paragraph 4. The policies and procedures set by the firm are out of the direct control of the engagement partner or the engagement quality reviewer. If, for example, the firm does not have the requisite policies and procedures in place, but the engagement quality reviewer otherwise performs the engagement quality review with competence, independence, integrity, and objectivity and in accordance with the standards of the PCAOB, then technically, the engagement still would not have been performed in accordance with the auditing standards.

As a result, we also would support updating the PCAOB's interim Quality Control standards, which establish standards regarding a firm's responsibilities for its system of quality control. Examples of requirements that would be appropriate to house in the Quality Control standards are:

- The requirement for the tone set at the top of the firm to encourage and support the performance of objective engagement quality reviews, which will be "lost" when this proposed standard supersedes SECPS Requirements of Membership §100.08(f); and
- The requirement for the firm's quality control policies and procedures to include provisions to provide the firm with reasonable assurance that the engagement quality reviewer has sufficient competence, independence, integrity, and objectivity to perform the engagement quality review in accordance with the standards of the PCAOB, which is misplaced in a note to paragraph 4 of the proposed standard.

With respect to the note to paragraph 4, we suggest either deleting the note, or referring to the requirement in the Board's interim quality control standards.

We believe that housing the firm's requirements in the Quality Control standards, and the auditor's requirements in the auditing standards and the attestation standards, as appropriate, lends clarity to the requirements, and in particular, who is responsible for compliance with the requirements, in the respective standards.

Qualifications of the engagement quality reviewer

We continue to support the provision that an engagement quality reviewer should be an associated person of a registered public accounting firm, and that he or she should have competence, independence, integrity and objectivity.

Objectivity

We agree with the proposal to allow an engagement quality reviewer to be a partner (or equivalent) of the firm, or an individual outside the firm. Although this might appear to reduce flexibility in smaller registered firms, we agree that, under ordinary circumstances, a non-partner in an accounting firm would not be qualified to conduct the engagement quality review, as measured against the requirements of this standard. Furthermore, we are sympathetic to the concerns that some commentators expressed regarding the authority that a non-partner in the firm would have in conducting an objective review of the engagement partner's work.

We believe that the Board has found a sensible solution by requiring in-house engagement quality reviewers to be partners (or equivalents), while allowing engagement quality reviewers from outside the firm to come from a variety of backgrounds. This solution mitigates the concerns regarding the authority of in-house engagement quality reviewers. At the same time, it does not inappropriately limit the available qualified resources from outside the firm.

We support changes made to the standard to clarify the requirement for the engagement quality reviewer to remain objective. Specifically, we believe:

- the changes in paragraph 6 appropriately define “objectivity” in terms of the engagement, and not in terms of the engagement team;
- the removal of the note to paragraph 6 (now paragraph 7) eliminates the perception that the standard would limit consultation between the engagement team and the engagement quality reviewer. We believe that consultation is an important element of audit quality, and that these changes encourage appropriate consultation without compromising the objectivity of the engagement quality reviewer; and
- the language added to paragraph 7(c) clarifies that the engagement quality reviewer may not supervise the engagement team with respect to the engagement under review, but may otherwise be partners with leadership and supervisory responsibilities in the firm.

Further, we agree that it would be more difficult for an engagement partner, who has had overall responsibility for the audit for a year or more, to perform the review with the level of objectivity of someone who is new to the engagement. Accordingly, we support the new requirement that the engagement quality reviewer may not be the person who had overall responsibility for either of the two audits preceding the audit subject to the engagement quality review.

Competence

With respect to the description of what constitutes a competent engagement quality reviewer, the language on page 12 of the release, and removal of the “oil and gas” example in the original

proposal, which implied that the engagement quality reviewer had to have experience sufficient to serve as the engagement partner for the audit of a company in the industry, go a long way toward clarifying that the engagement quality reviewer need not be a “clone” of the engagement partner. Nevertheless, we believe further clarification is needed. There may be substantial overlap between the skills required of the engagement partner and the skills required of the engagement quality reviewer, but it is not the exact same skill set that is required by both.

Paragraph 5 of the proposal indicates that the engagement quality reviewer must possess the competence to serve as the engagement partner for the same type of engagement. We believe it is more important that the engagement quality reviewer possess the competence to serve as the engagement quality reviewer. We would propose the following statement regarding the competence of the engagement quality reviewer:

Competence The engagement quality reviewer must possess the level of technical knowledge and competence relating to accounting, auditing, and financial reporting required to [review] the significant judgments made by the engagement team and the conclusions reached in forming the overall conclusion on the engagement and in preparing the engagement report, if a report is to be issued, in order to determine whether to provide concurring approval of issuance.

Note: The determination of what constitutes the appropriate level of technical knowledge and competence should be based on the circumstances of the engagement, including the size or complexity of the business¹.

Note: Considerations in evaluating competence include, but are not limited to, technical expertise, experience, knowledge of SEC rules and regulations pertinent to the engagement, and industry knowledge.

Concurring approval of issuance

On page 16 of the release accompanying the first proposal, it is acknowledged that differences of opinion could occur between the engagement team and the engagement quality reviewer, and that, if those differences have not been satisfactorily resolved, the engagement quality reviewer must not provide concurring approval. We continue to believe that this resolution of differences is an important contributor to audit quality, but the concept is not addressed in the proposed standard itself. We suggest that the standard state that, if one of the four conditions in paragraph 12 exists, and those differences have not been satisfactorily resolved, the engagement quality reviewer must not provide concurring approval.

Although we believe that the resolution of difference of opinion between the engagement team and the engagement quality reviewer is an important contributor to audit quality, we do not believe that the fact that there have been such differences is an indicator of audit quality, or a lack thereof. The engagement quality review process is one of the internal processes by which the firm monitors the quality of its audits. Therefore, we would caution the board against

¹ This sentence is from the first proposal, footnote 18.

requiring the communication of any differences of opinion between the engagement team and the engagement quality reviewer to those outside the firm.

We believe that such a requirement would limit consultation between the engagement team and the engagement quality reviewer, which potentially would reduce audit quality. Furthermore, we do not believe that it would provide meaningful information to management or those charged with governance of the entity being audited. Finally, we believe that it may cause confusion among users, who may conclude that the entire firm is not behind the report. It may also incorrectly signal to users and the markets that auditing is an individual effort, rather than a multi-faceted collective enterprise involving many experts in many disciplines, with numerous institutional checks and controls.

Documentation of an engagement quality review

It is not clear to us if the discussions meant to be captured by the requirement in paragraph 19(c) are those among the members of the engagement quality review team, or those between the engagement quality review team and the engagement team. In either case, it seems like it would be an inordinate amount of documentation, especially since the specificity of the requirement to document “date of each discussion, the specific matters discussed, the substance of the discussion, and the participants,” goes beyond the requirements to document discussions in AS No. 3. Furthermore, since the significance of the discussion may not be clear when the discussion begins, we believe this requirement would result in the transcribing of many discussions that, at the end of the engagement, turn out not to be significant.

Assuming that the discussions meant to be captured are those between the engagement quality reviewer and the engagement team, we believe that the essence of the discussions would have been required to have been documented by the engagement team in accordance with AS No. 3, making this requirement redundant. We recommend amending paragraph 19(c) to apply to significant discussions between the engagement quality reviewer and the engagement team that have not otherwise been documented by the engagement team. We further recommend that the language in footnote 36 of the Release, which explains what constitutes a “significant discussion,” be included in the final standard.

Effective date

As proposed, the standard would be effective for audits of fiscal years ending on or after December 15, 2009, and for interim reviews for fiscal years beginning after December 15, 2009. Because the SEC is unlikely to approve this standard before the end of the second quarter of 2009, this effective date would result in the engagements to perform interim reviews on the first two or three quarters of 2009 being reviewed under the extant standard, while the audit, and perhaps the third quarter interim review would be reviewed under this standard as finalized. Furthermore, we will have begun planning for some of our December 31, 2009 audits before this proposed standard is finalized. In this event, firms would be required to perform interim reviews and planning December 31, 2009 audits using their best guess as to the form of the final standard. We do not believe that introducing this uncertainty and potential variance in practice is desirable. We recommend that the PCAOB set the effective date for audits and interim reviews to annual periods beginning no earlier than twelve months after SEC approval.

Content and structure of the standards

The Sarbanes-Oxley Act of 2002 requires the PCAOB to establish auditing, related attestation, and quality control standards. We believe that some thought should be put into the structure of the standards, and how they relate to each other, before the Board goes much further down one path or the other.

In the context of providing comments on the PCAOB's proposed standard, we supported the proposal to limit the application of this standard to audit engagements and engagements to review interim financial information. We did so because we believe that the requirements in the proposed standard are so specific to those engagements that it would be difficult to adapt them to other types of engagements. Furthermore, we believe that, because it is contained in the auditing standards, it should only apply to the engagements to which the auditing standards apply. The logical extension of this approach would be, if the Board believes engagement quality reviews are desirable for attestation engagements, those requirements should be established in an attestation standard rather than an auditing standard.

However, we believe the engagement quality review should be considered in the context of all the elements of quality control, for example, consultation, supervision, and training, and not as an independent issue. We believe it would be appropriate for the standards on those topics to be included together in the quality control standards. We believe that keeping this proposed standard in the auditing standard perpetuates the misperception that the engagement quality review compensates for lapses in other aspects of quality control.

Convergence with international standards

We found the comparison to the International Standards on Auditing in the PCAOB's proposed *Auditing Standards Related to the Auditor's Assessment of and Response to Risk* to be very helpful; we missed a similar comparison in this proposed standard. We believe it would be good practice for the PCAOB to publish such comparisons in all of its proposals and final standards. To understand what the PCAOB considers (and does not consider) to be a significant difference helps clarify the meaning of the standard and the intent of the Board.

We would like to again express our recommendation that the Board consider the feasibility of adopting the ISAs as a base. In doing so, PCAOB standards can be focused on the incremental requirements that would be necessary for audits of issuers.

Paragraph-level comments

The following offers specific paragraph-level comments for the Board's consideration.

Paragraph	Comment
7(b)	While we understand the clear need for independence of the engagement quality reviewer, words like "any" are absolute and must be used with caution given the potential for unintended consequences. Such is the case in paragraph 7(b). Given the very broad and diverse activities that the word "responsibilities" encompasses, indicating that the engagement quality reviewer should not "assume any of the responsibilities of the engagement team" could lead to potential violations of this requirement for insignificant or inconsequential matters or for matters where efficiencies could be gained.

Paragraph	Comment
9	This paragraph does not make clear the fact that the engagement quality reviewer is not required to review each and every piece of audit documentation, but rather the selected documentation that the engagement quality reviewer considers necessary to identify and evaluate the significant judgments and conclusions. We propose the following language: "...and by reviewing documentation <u>that the engagement quality reviewer considers necessary.</u> "
12	With respect to the note in this paragraph, we believe that the overall conclusion on the subject matter of the engagement is expressed in the engagement report. That is, if the overall conclusion was incorrect, the engagement report would be inappropriate. If we are correct in our understanding, we suggest that items (2) and (3) in the note to this paragraph be combined. If we are incorrect, we suggest that these items be clarified.
17	This paragraph provides guidance to the engagement quality reviewer as to when he or she may provide concurring approval of issuance in a review of interim financial information. However, often, in the case of a review of interim financial information, a report is not "issued."

We would be pleased to discuss this letter with you. If you have any questions, please contact Mr. John L. Archambault, National Managing Partner of Professional Standards, at (312) 602-8701.

Sincerely,





April 20, 2009

Office of the Secretary
PCAOB
1666 K Street, N.W.
Washington, D.C. 20006-2803

Re: PCAOB Rulemaking Docket Matter No. 025

Dear Sir/Madam:

The Audit and Assurance Services Committee of the Illinois CPA Society (“Committee”) is pleased to comment on the Reproposed Auditing Standard, *Engagement Quality Review*.

The Committee is a voluntary group of CPAs from public practice, industry, education and government. Our comments represent the collective views of the Committee members and not the individual views of the members or the organizations with which they are affiliated. The organization and operating procedures of our Committee are outlined in Appendix A to this letter.

The Committee approves of the approach of the PCAOB to improve the quality of concurring reviews and established standards for its performance. Furthermore, the Committee acknowledges and appreciates the Board’s thoughtful consideration of the comment letters received on its initial proposal and the changes made to the proposed standard in response to those comments.

The following responses to the eleven specific questions contained in the proposed standard reflect the consensus of the committee members except where indicated:

1. The standard should not require an EQR for other kinds of engagements performed according to PCAOB standards.
2. The objective of the repropoed standard is appropriately formulated and articulates the purpose of an EQR.
3. The objective will contribute to a more thoughtful and effective EQR.
4. The proposed standard would require an in-house EQR reviewer be a partner or a person in an equivalent position, and expressly exclude a person at the manager level. While the proposed standard defines who is not in an “equivalent” position, it leaves it unclear as to who would be in such an

equivalent position. Would this be a “senior” manager? Firms should not be left to guess if someone besides a partner qualifies. This term, equivalent position, should be better defined through the use of examples.

A majority of our Committee (hereinafter referred to as “we”) also want to comment about the stated concern surrounding the use, as a reviewer, of a non-partner within the firm. The institutionalizing, in this standard, of the concept that influence and/or intimidation might overcome the due professional care and other ethical standards that are central to all audits is very troubling. To the extent such issues could impact the EQR process, there is no reason to believe that one partner could not also be influenced or intimidated by a more senior partner, as the Board recognizes in their discussion.

We believe that competence is the most important qualification beyond independence, integrity and objectivity. Technical competence can certainly exist in a non-partner within the firm. In fact, given the economics that exist in public accounting as well as other professions, technical competence is often not sufficient to allow a CPA to ascend to partnership in a CPA firm. It is likely that business growth skills will outweigh technical competence in decisions to elevate a person to partner. It can be argued that a technically competent manager will be less susceptible to influence and/or intimidation than a partner whose income may be more closely tied to the ability to satisfy a client’s needs.

However, this dynamic should not be vetted in an audit standard. It is demeaning to the profession in general, and to all CPAs individually. The focus should be on who is capable of performing the reviewer role, not on the possibility that someone may prove to be unable to perform the function. As we have all seen in recent months, from one financial fraud to the next, the appearance of integrity, propriety and honesty as a result of reputation and position has been no guarantee of those traits.

Finally, we believe that smaller firms will be unduly burdened with the requirement to use a partner as the reviewer. They will need to have two partners who are sufficiently competent to perform the review, and not have the flexibility to utilize a competent manager. While it is true that they can go outside the firm for retired partners, professors of auditing or other qualified accountants, this will add costs to the engagement that will either increase the cost of the EQR to their client, or reduce the profitability to the firm. In either case, their competitiveness with other larger firms is adversely impacted. As a result, it is possible that this requirement might reduce the number of firms capable of providing audit services in this market.

A minority of the Committee does believe that the Board’s proposal to only allow partners or persons in an equivalent position is appropriate.

5. The standard should allow qualified accountants who are not employed by an accounting firm to conduct a review.

6. The standard should prohibit the engagement partner from serving as the reviewer for at least two years following their last year as the engagement partner.
7. The descriptions of the scope and extent of EQR procedures contained in the repropoed standard are appropriate and will result in a high-quality EQR if properly performed.
8. The specifically required procedures are appropriately tailored to reflect the difference in scope between an audit and an interim review.
9. The specifically required procedures sufficiently focus the review on the areas of highest risk. No other procedures should be required.
10. The standard for the engagement quality reviewer's concurring approval of issuance is appropriately described in the repropoed standard. The first condition is appropriately tailored to reflect the difference in scope between an audit and an interim review.
11. The documentation requirements enumerated in paragraphs 19(a), 19(b) and 19(d) of the repropoed standard are appropriate. However, the requirement of paragraph 19(c) that significant discussion held by the engagement quality reviewer and others who assisted the reviewer be documented raises several issues.

The repropoed standard contains no definition or criteria as to what constitutes a "significant discussion". This creates the potential for varying interpretations across the profession. Firms which define "significant discussion" narrowly may discourage communication with the engagement quality reviewer due to a perceived documentation requirement. This, in turn, would likely reduce the effectiveness of the EQR.

Also, considering audit documentation requirements under AS3, it is difficult to imagine a circumstance in which an engagement quality reviewer or his assistants would need to rely upon matters voiced in a "significant discussion" to achieve their objective and still conclude that the engagement team obtained sufficient appropriate audit evidence. In other words, if an engagement quality reviewer finds it necessary to have a "significant discussion" with the engagement team in order to evaluate the significant judgments made by the engagement team and the conclusions reached in forming the overall conclusion on the engagement, how could an experienced auditor, having no previous connection with the engagement, evaluate these conclusions?

If the Board retains the requirement of paragraph 19(c), the term "significant discussions" should be clearly defined through the use of specific criteria and examples.

The Illinois CPA Society appreciates the opportunity to express its opinion on this matter.
We would be pleased to discuss our comments in greater detail if requested.

Sincerely,

A handwritten signature in black ink, reading "Jon Hoffmeister". The signature is written in a cursive style with a horizontal line extending from the end of the name.

Jon R. Hoffmeister, Chair
Audit and Assurance Services Committee

APPENDIX A

ILLINOIS CPA SOCIETY
 AUDIT AND ASSURANCE SERVICES COMMITTEE
 ORGANIZATION AND OPERATING PROCEDURES
 2008 – 2009

The Audit and Assurance Services Committee of the Illinois CPA Society (Committee) is composed of the following technically qualified, experienced members appointed from industry, education and public accounting. These members have Committee service ranging from newly appointed to more than 20 years. The Committee is an appointed senior technical committee of the Society and has been delegated the authority to issue written positions representing the Society on matters regarding the setting of audit and attestation standards. The Committee's comments reflect solely the views of the Committee, and do not purport to represent the views of their business affiliations.

The Committee usually operates by assigning Subcommittees of its members to study and discuss fully exposure documents proposing additions to or revisions of audit and attestation standards. The Subcommittee develops a proposed response that is considered, discussed and voted on by the full Committee. Support by the full Committee then results in the issuance of a formal response, which at times includes a minority viewpoint.

Current members of the Committee and their business affiliations are as follows:

Public Accounting Firms:**Large:** (national & regional)

Peggy L. Brady, CPA	McGladrey & Pullen LLP
Matthew L. Brenner, CPA	PricewaterhouseCoopers LLP
Jeffrey A. Gordon, CPA	KPMG LLP
Jon R. Hoffmeister, CPA	Clifton Gunderson LLP
Neil F. Finn, CPA	Deloitte & Touche LLP
William P. Graf, CPA	Deloitte & Touche LLP
Michael J. Pierce, CPA	McGladrey & Pullen LLP
Kevin V. Wydra, CPA	Crowe Horwath LLP

Medium: (more than 40 employees)

Damitha N. Bandara, CPA	Blackman Kallick LLP
Sharon J. Gregor, CPA	Selden Fox, Ltd.
Stephen R. Panfil, CPA	Bansley & Kiener LLP
Jennifer E. Sanderson, CPA	Frost, Ruttenberg & Rothblatt, P.C.

Small: (less than 40 employees)

James R. Adler, CPA	Adler Consulting Ltd.
Scott P. Bailey, CPA	Bronner Group LLC
Loren B. Kramer, CPA	Kramer Consulting Services, Inc.
Andrea L. Krueger, CPA	Corbett, Duncan & Hubly P.C.
Ludella Lewis	Ludella Lewis & Company
Richard D. Spiegel, CPA	Steinberg Advisors, Ltd.

Industry:

Nicole G. Kiriakopoulos, CPA	Stericycle, Inc.
Janis D. Potter, CPA	MTL Insurance Co.

Staff Representative:

Paul E. Pierson, CPA	Illinois CPA Society
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Office of the Secretary
 PCAOB
 1666 K Street N.W.
 Washington D.C. 20006-2803
 USA

By E-mail: comments@pcaobus.org

April 20, 2009

Dear Sir(s):

**Re.: PCAOB Rulemaking Docket Matter No. 025
 PCAOB Release No. 2009-001
 Reproposed Auditing Standard – Engagement Quality Review**

The Institut der Wirtschaftsprüfer in Deutschland [Institute of Public Auditors in Germany], appreciates the opportunity to comment on the above-mentioned Reproposed Auditing Standard – Engagement Quality Review (hereinafter referred to as the “reproposed standard”).

We support the Board’s revising the draft standard issued for comment in 2008, and on the whole, agree that the changes now proposed constitute significant improvement. We continue to share the Board’s view that well-performed engagement quality reviews are an important element in establishing a basis for investor reliance on audits and agree with the aims of the reproposed PCAOB auditing standard. Nevertheless, we do have some major residual concerns which we discuss below. In the Appendix to this letter we respond to the questions posed by the Board.

Major concerns

Applicability

In our comment letter dated May 12, 2008, relating to the proposed Auditing Standard on Engagement Quality Review, PCAOB Release No. 2008-002 of the same docket number, we had commented on the applicability of the proposed

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GESCHÄFTSFÜHRENDER VORSTAND:
 Prof. Dr. Klaus-Peter Naumann,
 WP StB, Sprecher des Vorstands;
 Dr. Klaus-Peter Feld, WP StB CPA;
 Manfred Hamann, RA



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standard, comparing the [then] proposed applicability: "...for each engagement performed and completed in accordance with the standards of the PCAOB" to the approach taken by the IAASB in its quality control standard. The approach in the repropoed standard seems to be somewhat arbitrary in requiring an engagement quality review be performed for all audit engagements and all reviews of financial information ("interim reviews") but *no* other engagements carried out in accordance with the standards of the PCAOB. We continue to believe there may be merit in adopting a more risk-based approach in a manner similar to that adopted by the IAASB, and, in this context, would like to refer to our earlier letter.

Reviewer qualifications

We had also commented on this issue in the afore-mentioned letter, as follows:

"We support the proposal that suitably qualified persons both not necessarily at partner level and also external to the firm may perform engagement quality reviews. This allows more flexibility than current PCAOB's interim requirements, and is likely to be particularly helpful to smaller foreign registered firms seeking suitable engagement quality reviewers.

However, we note that the levels of knowledge and competence that an engagement quality reviewer must possess according to the proposed standard are more stringent than those stipulated in the PCAOB's interim requirements and by the IAASB in its counterpart standards¹. The proposals require the experience of the quality control reviewer to be sufficient to enable him or her to serve as engagement partner in the specialized industry (we refer to page 9 of the Release). This may be problematical for foreign audit firms, and in particular smaller firms, where the "pool" of potential engagement quality reviewers may be limited".

We are concerned as to the changes made to paragraph 3 (formerly paragraph 2), which now clarify that "another individual in the firm" has to be "in an equivalent position in the firm" to that of the engagement partner. The Board's argument that only a partner or another individual in an equal position in the firm will have requisite authority does not seem to us to be sufficiently persuasive, since a partner within the same firm as the engagement partner may be subject to the

¹ [Proposed] ISQC 1 (Redrafted) paragraph A42 states that for an audit of a listed entity the engagement quality control reviewer "... would be an individual with sufficient and appropriate experience and authority to act as an audit engagement partner on audits of financial statements of listed entities."



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same firm internal pressures. In addition, it is questionable why a reviewer from outside the firm can – per se – be considered to have the requisite level of authority which a non-partner from inside the firm would lack. We believe that both technical expertise and experience ought to remain prerequisites for reviewers, as is the case currently. Indeed, in our opinion, the necessary practical experience ought to be appropriate but also recent. The examples cited on page 12 of the release: “retired partners, professors of auditing, or other qualified accountants” will not necessarily fulfill such criteria.

We generally support the introduction of the new restriction in paragraph 8 of the repropoed standard as we appreciate the considerations relating to objectivity and the familiarity threats that may arise. However, we would like to point out that both IFAC’s IESBA and IAASB have adopted a more flexible approach in addressing this issue. For example, section 290.154 b of the IFAC Code of Ethics stipulates: “Such an individual [engagement partner or individual responsible for the engagement quality control review] rotating after a pre-defined period should not participate in the audit engagement until a further period of time, normally two years, has elapsed.” Section 290.157 recognizes: “When a firm has only a few people with the necessary knowledge and experience to serve as engagement partner or individual responsible for the engagement quality control review on a financial statement audit client that is a listed entity, rotation may not be an appropriate safeguard.” ISQC 1 requires the firm to establish policies and procedures designed to maintain the objectivity of the engagement quality control reviewer. These can be tailored to the individual circumstances of the firm. Therefore, we suggest that it may be appropriate for the Board to include some degree of flexibility in a similar manner.

Respective Authorities

We are concerned that the repropoed standard still does not clarify the respective responsibilities of the engagement partner and the engagement quality reviewer, nor does it stipulate how conflicting views between the engagement quality reviewer and the engagement partner are to be dealt with such that the firm will be in a position to grant permission to the client to use the engagement report. In this context we also refer to the afore-mentioned letter in which we commented on these issues in more detail.



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We would be very pleased to be of further assistance if you have any questions or comments about the content of our letter.

Yours truly,

Klaus-Peter Feld
Executive Director
541/500

Ulrich Schneiss
Director Auditing

Encl.: Appendix



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APPENDIX

Specific questions raised by the PCAOB in PCAOB Release No. 2009-001:

1. *Should the standard require an EQR for other kinds of engagements performed according to PCAOB standards? If so, what types of engagements should be included and what should an EQR of such engagements entail?*

We refer to our comments on major concerns in the accompanying letter.

2. *Is the objective in the repropoed standard appropriately formulated? Does it articulate the purpose of an EQR?*

We note that the IAASB's recently revised and redrafted ISQC 1 defines an engagement quality control review as "A process designed to provide an objective evaluation...". In our opinion, in view of the fact that the engagement quality reviewer must be an associated person of a registered firm, it is important to stress that the evaluation by a quality reviewer of those significant judgments and related conclusions reached by an engagement team needs to be objective. We therefore suggest this aspect be made clear in the objective paragraph 2. This is in line with paragraph 6 which states: "... the engagement quality reviewer must ... maintain objectivity in performing the review."

3. *Will this objective contribute to a more thoughtful and effective EQR?*

As stated in our previous letter we support the inclusion of an objective.

4. *Is it appropriate to explicitly require a reviewer from within the firm to be a partner or an individual in an equivalent position?*

We refer to our comments on major concerns in the accompanying letter.

5. *Should the standard allow qualified accountants who are not employed by an accounting firm to conduct the review?*

We refer to our comments on major concerns in the accompanying letter.



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6. *Should the standard prohibit the engagement partner from serving as the reviewer for a period of time following his or her last year as the engagement partner? If so, is two years sufficient, or should it be extended?*

We refer to our comments on major concerns in the accompanying letter. We also agree that the cooling-off period should not exceed two years.

7. *Are the descriptions of the scope and extent of EQR procedures contained in the repropoed standard appropriate? Will the performance of these procedures result in a high-quality EQR? If not, how should these procedures be revised?*

In stipulating the procedures to be performed in paragraphs 9, 10, 14 and 15 the Board makes no specific mention as to how the reviewer should take account of materiality.

8. *Are the specifically required procedures appropriately tailored to reflect the difference in scope between an audit and an interim review?*

In our opinion, paragraph 15 needs to be more closely brought in line with the procedures required in an engagement to review interim financial information. For example, given the fact that a review is likely to be less effective than an audit in respect of fraud identification, it is not clear to us why the Board requires the engagement quality reviewer to concentrate on “identified risks of material misstatement due to fraud” (3rd bullet in paragraph 15.a.) when, according to the PCAOB’s interim standard, the reviewer is required to have “sufficient knowledge of the entity’s business and its internal control to identify the types of potential material misstatements in the interim financial information and consider the likelihood of their occurrence”. Furthermore, rather than simply including the procedures in paragraphs 10.c.-f. within paragraph 15.b. as quality review procedures for interim review engagements, we suggest there is a need for similar procedures tailored to interim reviews. In particular paragraph 10.d. needs to be aligned to the work performed in an interim review engagement. As the relevant Board’s interim standard states: “A review is not designed to provide assurance on internal control or to identify significant deficiencies. However, the accountant is responsible for communicating with the audit committee or others with equivalent authority or responsibility, regarding any significant deficiencies that come to his or her attention.” Review engagements may not identify control deficiencies as would be the case in an audit such that evaluation of judgments made about the severity and disposition of identified control deficiencies cannot be comparable in reviewing an audit, and a review engagement respectively.



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9. *Do the specifically required procedures sufficiently focus the reviewer on areas of highest risk? Are there other procedures that should be required?*

We refer to our response to question 8.

10. *Is the standard for the engagement quality reviewer's concurring approval of issuance appropriately described in the reproposed standard? Is the first condition appropriately tailored to reflect the difference in scope between an audit and an interim review?*

We would like to point out that the wording of paragraphs 13 and 18 respectively may cause some confusion, since both refer to the firm granting permission to the client to use the engagement report rather than the firm issuing the engagement report. It begs the question can the report have been previously issued pending such permission prior to completion of the engagement quality review? We presume that this is not the Board's intention.

In our opinion, the differentiation is appropriate.

11. *Are the documentation requirements in the reproposed standard appropriate? If not, how should they be changed?*

In our opinion, the documentation requirements are appropriate.



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April 20, 2009

Office of the Secretary
Public Company Accounting Oversight Board
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Washington, D.C. 20006-2803

PCAOB Rulemaking Docket Matter No. 025
Proposed Auditing Standard, *Engagement Quality Review*

Dear Mr. Secretary:

KPMG appreciates the opportunity to comment on the Public Company Accounting Oversight Board's (PCAOB or the Board) Release No. 2009-001 (the Release), which includes the Proposed Auditing Standard, *Engagement Quality Review* (the Proposed Standard), and we commend the Board for seeking further comment on the proposal.

We agree with the Board that a well-performed engagement quality review is an important element of audit quality. The Board explains in the Release that an engagement quality review standard should focus on the need to perform a robust review, must require a review that serves in a meaningful way to identify significant engagement deficiencies in time to correct them, and should provide a safeguard against erroneous or insufficiently supported opinions.¹ We believe the Proposed Standard's requirements are generally consistent with these objectives. We also believe a final standard substantively consistent with the Proposed Standard will promote improvements in audit quality without requiring a re-audit.²

While we support a rigorous engagement quality review standard, we recommend that the Board clarify certain of the engagement quality review requirements to ensure that the implementation

¹Release page 3, "The Board generally agreed that new requirements are necessary to focus reviewers on the need to perform a robust review rather than on whether particular matters had come 'to [their] attention'. Release page 4, "At the same time, the Board continues to believe that in order to improve audit quality, the standard must require an EQR that serves as a meaningful way to identify significant engagement deficiencies in time to correct them." Release page 15, "On the other hand, too narrow a scope could result in reviews that do not provide a safeguard against erroneous or insufficiently supported audit opinions."

² Release page 15 states that "At the same time, the Board recognized that an effective review need not – and should not – amount to a re-audit, and that the role of a reviewer differs significantly from that of an engagement partner."



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of the final standard is effective and consistent with the Board's intent. We believe that the Proposed Standard contains requirements that are unnecessary for the reviewer to achieve the engagement quality review objective in the Proposed Standard and may not be cost-effective.³ We recommend that the Board revise or eliminate these requirements. We also believe that the effective date of the final standard should reflect the time necessary to train firm engagement quality reviewers and engagement team members on the standard's requirements and to modify audit methodologies and work papers in a manner that promotes effective implementation. Specifics on these recommendations are provided in the remainder of this letter.

Clarify the Requirements of the Engagement Quality Review Process

We support the Proposed Standard's presentation of separate engagement quality review process requirements for audit and review engagements. This approach enables the Board to supplement the broadly articulated requirements, such as those in the objective (paragraph 2) and the general descriptions of the engagement quality review process (paragraphs 9 and 14), with the detailed requirements necessary for consistent and effective implementation. We also support the Proposed Standard's statement that the reviewer performs the engagement quality review procedures through discussions with the engagement team and review of engagement documentation (paragraphs 9 and 14). We believe that these statements help clarify that the engagement quality review process does not require the reviewer to reperform the work performed by the engagement team or to seek out evidence beyond that which is gathered by the engagement team. However, the Board's intent with respect to both the objective and the specific requirements of the engagement quality review process for audit and review engagements should be clarified.

As drafted, the structure of the Proposed Standard implies that the objective and the related definition of significant engagement deficiency should inform the reviewer's judgments about the nature and extent of procedures necessary to comply with the engagement quality review process requirements for audit and review engagements. In this regard, even though the Proposed Standard only requires an evaluation of the engagement team's "significant judgments," it is unclear whether a significant judgment is any engagement team judgment that, if the reviewer disagrees, could lead to a significant engagement deficiency. As "significant engagement deficiency" is defined in the Proposed Standard, any engagement team judgment poses the risk of a significant engagement deficiency if it involves matters that are pervasive to the conduct of the engagement or impact the nature, timing or extent of procedures performed for significant accounts or disclosures (or components thereof that could be material to the entity's financial reporting). We recommend that the Board clarify how the Proposed Standard's objective, including the related definition of significant engagement deficiency, should impact the judgments a reviewer makes in determining the nature and extent of procedures necessary to

³ Paragraph 2 of the Proposed Standard states that, "The objective of the engagement quality reviewer is to perform an evaluation of the significant judgments made by the engagement team and the conclusions reached in forming the overall conclusion on the engagement and in preparing the engagement report, if a report is to be issued, in order to determine whether to provide concurring approval of issuance."



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identify and evaluate significant judgments (paragraphs 9 and 14) by performing the engagement quality review process requirements described in paragraphs 10 and 15.

In addition, we observed that the Proposed Standard continues to use “identify,” “evaluate” and “determine” to describe a reviewer’s responsibilities. These words connote that a reviewer makes his or her judgments with a higher degree of certainty than does the use of “review.” And while “identify,” “evaluate” and “determine” are also used to describe requirements in other standards of the Board (e.g., AS No. 5), those standards are complied with in the context of obtaining reasonable assurance about the reporting objective. In light of this difference, we believe the Board should clarify how it intends a reviewer’s judgments about the nature and scope of the procedures necessary to comply with the Proposed Standard’s “identify,” “evaluate” and “determine” requirements to be different from the judgments he or she would make in the role of an engagement partner to comply with similarly worded requirements in other standards of the Board. An engagement quality review process that requires the reviewer to comply with the requirements in the same manner as if he or she were serving as the engagement partner, rather than the engagement quality review partner, appears inconsistent with the statements in the Release which explain that the Board recognizes that the role of a reviewer differs significantly from that of an engagement partner.⁴

The following sections elaborate on these overall comments and highlight specific matters where we believe further clarification of the engagement quality review process is necessary.

Evaluations of Engagement Planning, Risk Assessments and Audit Responses in an Audit

The requirements in paragraphs 10(a) and 10(b) to *evaluate* engagement planning, risk assessments and audit responses likely will represent a significant increase in effort as compared to current concurring review practice. The breadth and depth of judgments made in an audit that constitute engagement planning, risk assessments and audit responses is significant. The Board’s recent proposals⁵ on the auditor’s assessment of and response to risk illustrate this point by explaining that engagement planning and risk assessment consist not only of matters pervasive to the conduct of the audit, but also the assessments of inherent, control, and detection risk made for individual assertions of significant accounts and disclosures and the corresponding judgments about what constitutes sufficient appropriate audit evidence and the nature, timing and extent of audit procedures necessary to obtain such evidence. Similarly, paragraph 10 of AS No. 5 explains that in an audit of internal control over financial reporting, “Risk assessment underlies

⁴ Release page 15 states that “At the same time, the Board recognized that an effective review need not – and should not – amount to a re-audit, and that the role of a reviewer differs significantly from that of an engagement partner.”

⁵ See PCAOB Release No. 2008-006 dated October 21, 2008 relating to PCAOB Rulemaking Docket Matter No. 026.



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the *entire* audit process described by this standard, including determination of significant accounts and disclosures and relevant assertions, the *selection of controls to test* and the *determination of the evidence necessary for a given control* (emphasis added).” Evaluations of the judgments of the engagement team related to engagement planning, risk assessments, and audit responses at the individual assertion level for significant accounts and disclosures would require a very detailed consideration of the engagement team’s work. For example, we observe that a requirement to evaluate control risk assessments in a financial statement audit or the judgments about which controls to test and the evidence necessary for a given control in an integrated audit would involve an evaluation of the detailed audit documentation supporting the team’s evaluation of the design and implementation of internal control.

We acknowledge the directive in paragraph 9 which explains that paragraphs 10(a) and 10(b) are performed to identify and evaluate “significant judgments,” however, we do not believe paragraph 9 effectively limits the nature and scope of procedures necessary to comply with paragraphs 10(a) and 10(b). As discussed above, what the Board intends to be considered a significant judgment is not sufficiently clear in the Proposed Standard. In addition, we believe the requirement for the reviewer to *identify* significant judgments is unclear. We believe the responsibility to identify (i.e., accumulate and present) significant judgments for the engagement quality review is that of the auditor with final responsibility for the engagement and not the engagement quality reviewer. This is particularly true when the judgments involve matters specific to relevant assertions of significant accounts or components thereof. As drafted, the Proposed Standard is not clear whether the Board intends the reviewer to review the engagement documentation supporting all engagement planning, risk assessments, and audit responses to identify those judgments that are, in the judgment of the engagement quality reviewer, “significant” and then evaluate whether the team’s conclusions for these judgments are reasonable or whether they may represent a deficiency that requires follow-up.⁶

As the preceding paragraphs illustrate, the requirements in paragraphs 9, 10(a) and 10(b) need further clarification. Depending on how the requirements in paragraphs 10(a) and 10(b) are interpreted, the effort required to implement and comply with the standard may vary significantly and, without further clarification, would not likely be implemented consistently. In addition, while the requirements in paragraphs 10(a) and 10(b) use “including” in a manner that highlights particular matters, it does not limit the scope of the evaluation to those matters listed. We recommend that the proposal be revised to clarify how the Board intends for paragraphs 9 and 10(a) and 10(b) to be implemented. In this regard, we recommend that the standard be revised to require that the engagement quality reviewer evaluate the significant judgments, as identified for the reviewer by the engagement team, that relate to engagement planning, risk assessments and

⁶ Release page 17 states “The specifically required procedures are intended to give the reviewer the necessary information to evaluate the engagement team’s significant judgments and conclusions, and like all audit procedures, they must be performed with due professional care and professional skepticism. Accordingly, when performance of the procedures suggests a deficiency or red flag that, if pursued, could preclude the reviewer from providing concurring approval of issuance, the reviewer must follow up and make sure the matter is resolved before providing concurring approval.”



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audit responses, and any additional significant judgments of the engagement team that the reviewer identifies when performing the other procedures set forth in the standard.

Evaluations of Engagement Planning in a Review of Interim Financial Information

Paragraph 15(a) directs the engagement quality reviewer to evaluate the engagement planning of the interim review engagement. We note that SAS No. 100, *Interim Financial Information*, explains that procedures for conducting a review of interim financial information should be tailored to the engagement based on the accountant's knowledge of an entity's internal control. Engagement quality reviewers ordinarily would not have the necessary knowledge base about internal control to effectively "evaluate" the engagement planning. We recommend that the standard be revised to more clearly explain how the engagement quality reviewer would comply with this requirement. We also observe that the concerns we expressed in the *Evaluations of Engagement Planning, Risk Assessments, and Audit Responses in an Audit* section above relating to the lack of clarity in the requirement to identify significant judgments also apply to the requirements for engagement quality reviews of interim financial information.

Evaluations of Engagement Documentation in a Review of Interim Financial Information

Paragraph 16(a) directs the engagement quality reviewer to evaluate whether the engagement documentation indicates the engagement team responded appropriately to *significant risks*. The concept of significant risks relates to audit engagements and is not discussed in SAS No. 100. It is unclear whether the Proposed Standard is intending for the significant risks identified in the most recent audit engagement to be considered in paragraph 16(a), or whether the Board intends for the engagement team to conclude on what represent significant risks each interim period. We recommend that the Board eliminate paragraph 16(a) from the final standard so that it does not create a performance requirement for engagement teams to identify significant risks in an SAS No. 100 interim review engagement in a standard whose objective is targeted at engagement quality reviews.

Determining the Appropriateness of Consultations that Have Taken Place and Matters Identified for Communication

We believe that the procedures set forth in paragraphs 10(e) and 10(f) which require the reviewer to "determine if appropriate matters have been communicated, or identified for communication" and "determine if appropriate consultations have taken place on difficult or contentious matters" could be interpreted to go beyond the other requirements of the Proposed Standard that are focused on the evaluation of the work performed by the engagement team. We believe that the procedures in paragraphs 10(e) and 10(f) of the Proposed Standard should be modified to indicate that the engagement quality reviewer should make an evaluation of the appropriateness of such matters based upon performing the other procedures set forth in the standard.



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We suggest that these two paragraphs be modified as follows:

e. ~~Determine if~~ Evaluate whether appropriate matters that are identified through the performance of the other engagement quality review procedures in this standard have been communicated, or identified for communication to the audit committee, management, and other parties, such as regulatory bodies.

f. ~~Determine if~~ Evaluate whether appropriate consultations have taken place on difficult or contentious matters that are identified through the performance of the other engagement quality review procedures in this standard. Review the documentation, including conclusions, of such consultations.

Alternatively, the Board could include these two procedures in a new paragraph which would follow paragraph 10 and clarify that the evaluation should be made based upon the results of all other procedures performed in accordance with this standard.

Concurring Approval in a Review of Interim Financial Information

As proposed, in a review of interim financial information, the engagement quality reviewer must read the engagement report only if it is filed with the SEC. The final standard should require the engagement quality reviewer to read such a report if issued. Also, given that engagement reports are not issued in every review of interim financial information, the final standard should refer to the engagement quality reviewer's "concurring approval," rather than "concurring approval of issuance."

Documentation of an Engagement Quality Review

Paragraph 19(c) requires that the engagement documentation include the significant discussions held by the engagement quality reviewer and others who assisted the reviewer, including the date of each discussion, the specific matters discussed, the substance of the discussion, and the participants. We believe that this requirement is unnecessary in light of the objective and requirements of AS No. 3. Furthermore, the engagement partner has ultimate responsibility for ensuring that engagement documentation supports the significant judgments made and related conclusions reached. As such, the effectiveness of AS No. 3 may be undermined by a requirement in the engagement quality review standard to document or otherwise supplement documentation of the engagement team's basis for significant judgments made and related conclusions reached. Moreover, maintaining responsibility for engagement documentation with the engagement team will ensure that it is prepared by those with the most knowledge and information and therefore promote audit effectiveness.

Additionally, we believe the requirement in paragraph 19(c) is unnecessarily burdensome, which will result in additional costs that are not likely to provide a commensurate benefit to audit



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quality. As a result, we recommend it be deleted. For example, an engagement quality reviewer ordinarily has frequent dialog with the engagement team during the course of an engagement. At the time of a discussion, it is unreasonable to expect the engagement quality reviewer to know whether documentation of such discussions will ultimately be necessary to demonstrate compliance with the engagement quality review standard as contemplated in footnote 36 of the Release. As a result, the proposal will likely lead to effort spent transcribing discussions that, by the time concurring approval of issuance is provided, are appropriately reflected in the engagement documentation prepared by the engagement team in order to comply with AS No. 3. In other situations, summaries of these discussions may later be determined unnecessary to demonstrate compliance with the engagement quality review standard because of additional information or documentation that becomes available.

Based on the foregoing, we recommend the Board revise the engagement quality review documentation requirements to leverage the engagement documentation prepared by the engagement team in accordance with AS No. 3. In this regard, we note that paragraph 19(b) is drafted in a manner that appropriately focuses the documentation requirements on documentation prepared by the engagement team. If the Board believes that it is necessary for the final standard to contain guidance to ensure that documentation is prepared for information provided to the engagement quality reviewer through discussions, we recommend that paragraph 19 be revised. These revisions should include:

- eliminating paragraph 19(c) and revising paragraph 19(b) to clarify that the “documents reviewed” should include engagement documentation that is prepared based on significant discussions between the engagement quality reviewer and the engagement team.
- adding the explanation in footnote 36 of the Release of what constitutes a ‘significant discussion’ in the final standard, and
- clarifying that the discussions for which the work papers may need to be supplemented are those between the engagement quality reviewer, including any assistants, and the engagement team, and not discussions between the engagement quality reviewer and his or her assistants.

Due Professional Care

We note the Proposed Standard’s requirement that the engagement quality reviewer “may provide concurring approval of issuance only if, after performing with due professional care the review required by this standard, he or she is not aware of a significant engagement deficiency.” However, we respectfully disagree with the Board’s suggestion in the Release that “the requirement to exercise due professional care imposes on a reviewer essentially the same requirement as the ‘knows, or should know based on the requirements of this standard’ formulation in the Board’s original proposal.”⁷ Due professional care has established and accepted meaning and therefore we believe that it is inappropriate for the Board to read into the

⁷ See Release at Page 24.



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due professional care standard an element that is not established by precedent and would continue to raise concerns among engagement quality reviewers about the Board's intent for their performance obligations.

Effective Date of the Proposed Standard

As proposed, the final standard would be effective for audits of fiscal years ending on or after December 15, 2009, and for interim reviews for fiscal years beginning after December 15, 2009.

As it relates to audits, we continue to believe that the effective date should be linked to the beginning of an audit engagement period. By linking the effective date to the beginning rather than the end of an audit engagement period, the new requirements would (1) be known and anticipated as of the beginning of the audit engagement period, (2) allow the assigned engagement quality reviewer to comply with the requirements, such as the proposed documentation provisions, throughout audit engagement planning and execution, and (3) apply equally to each interim review during an audit period to which the proposed standard applies.

Due to the anticipated timing of approval, we are also concerned that the proposed effective date for audits would not permit sufficient time for registered public accounting firms to provide sufficient training and develop appropriate tools to ensure effective and efficient implementation of the new engagement quality review requirements. The effective date should provide sufficient time for registered public accounting firms to (1) adopt policies and procedures consistent with the new standard, (2) train their personnel in the requirements of the new standard, (3) modify audit methodologies and work papers and (4) assign or engage qualified engagement quality reviewers consistent with each respective firm's system of quality control.

Accordingly, we believe the PCAOB should base the effective date on fiscal years beginning after December 15, 2009, if the SEC approves the final standard by September 2009, to provide adequate time for firms to prepare for adoption.

If you have any questions about our comments, please do not hesitate to contact Jon Fehleison, (212) 909-5491 (jongfehleison@kpmg.com) or Glen Davison, (212) 909-5839 (gdavison@kpmg.com).

Very truly yours,

KPMG LLP



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CC: PCAOB

Mark W. Olson, Chairman
Daniel L. Goelzer, Member
Wilis D. Gradison, Member
Steven B. Harris, Member
Charles D. Niemeier, Member
Martin F. Baumann, Chief Auditor

CC: SEC

Mary L. Schapiro, Chairman
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April 16, 2009

Office of the Secretary, PCAOB,
1666 K Street, N.W.,
Washington, D.C. 20006-2803

RE: PCAOB Rulemaking Docket Matter No. 025

Dear Board,

We are writing in response to a request for comments regarding the proposed auditing standard for Engagement Quality Review. As a small firm we are very much interested in and affected by these rules so we appreciate the opportunity to make comments.

Being a small firm we naturally have a potential need to branch outside our partner group in order to appropriately satisfy the rules of partner rotation while still maintaining desired quality. We agree that it would not be appropriate to rely on review work from others in the firm who are less experienced, such as those at a level of manager or below. However, we have the opportunity to engage a retired partner from a large international firm, who is well qualified and has the experience necessary to perform engagement quality reviews. Although, he is interested in and willing to provide that service, he is not interested in being involved as an active "partner" in our firm. Utilizing such a person, or similarly qualified individuals, either from the profession or from academia seems consistent with speech comments made in connection with the re-release of the proposed standard--given March 4, 2009.

In utilizing such a person as described above, we feel that the objective of achieving quality and competent review would be better satisfied than by using other alternatives. For example, bringing in this type of person may be more effective than trying to cross train a tax partner to review public company audits, or even more appropriate than trying to involve a peer firm audit partner who may be reluctant or unable to dedicate the appropriate amount of effort.

With respect to ensuring responsible output, we observe that a qualified person as described above, although not an owner in our firm, still has a lifelong reputation as well as individual licensure at risk. Furthermore, being associated with our firm as a part or even a full-time employee, their work would naturally be subject to PCAOB inspection.

Please consider including language in the standard which will provide the use of appropriately qualified non-partner or non-owners of a small firm as candidates for engagement quality reviewers. We are happy to discuss these issues further as you may desire. Please feel free to contact Jon Lelegren, Mark Sperry, or Kim McReynolds at (801) 269-1818. Again, we appreciate the opportunity to submit our comments on this issue.

Sincerely,

A handwritten signature in black ink that reads "Jon E. Lelegren".

Jon E. Lelegren, Assurance Partner
Mantyla McReynolds, LLC

**Mayer Hoffman McCann P.C.**

An Independent CPA Firm

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April 21, 2009

Office of the Secretary
PCAOB
1666 K Street NW
Washington, D.C. 20006-2803

Re: PCAOB Rulemaking Docket Matter No. 025

We are pleased to have this opportunity to present the comments of Mayer Hoffman McCann P.C. (MHM) in response to the questions raised in the PCAOB's revised proposed auditing standard for engagement quality review included in PCAOB Release No. 2009-001 issued on March 4, 2009. Though MHM, in association with CBIZ, is listed by Accounting Today as the eighth largest accounting services provider in the U.S., we are a relatively new entity representing an amalgamation of many smaller CPA firms. We have a growing SEC practice and are committed to maintaining the high level of service we offer to our existing and future clients. We have created a culture revolving around a strong national office group which is actively involved in the designation of audit shareholders and concurring (engagement quality) reviewers for each of our SEC clients. We continue to agree with many of the concepts discussed in the release and are pleased that many of the comments we expressed in our letter dated May 9, 2008, were addressed by the PCAOB in the revised proposal on which the content of this letter relates.

As you have requested, we will follow the format of your questions and provide our comments in what we believe is the appropriate response to the question.

Applicability of the EQR Requirement

Question 1 – *Should the standard require an EQR for other kinds of engagements performed according to PCAOB standards? If so, what types of engagements should be included and what should an EQR of such engagements entail?*

We believe that an EQR should be performed for other types of engagements. As mentioned in the PCAOB's release, the primary engagements excluded from the scope of the new proposal are engagements performed under Auditing Standard No. 4, "Reporting on Whether a Previously Reported Material Weakness Continues to Exist" (AS 4) and engagements required by the SEC's Regulation AB. As our firm does not currently participate in engagements under Regulation AB, we have no specific comment on the scope of the EQR relative to those

engagements. In matters related to reports issued pursuant to AS 4, we believe that the EQR should be required to do the following (at a minimum):

1. From discussions with the engagement team:
 - a. Obtain an understanding of the nature of the material weakness(es) previously reported
 - b. Obtain an understanding of the changes in internal controls made by the company to remedy the material weakness(es) and how those changes are expected to eliminate the internal control deficiencies
 - c. Obtain an understanding of the engagement team's planned approach, expected scope and the extent of available evidence from the company
2. Evaluate the information obtained in step 1 (above) and the engagement team's judgments as to the sufficiency of the planned approach
3. Evaluate the engagement team's judgments with respect to the impact of the changes made by the client to the design and operating effectiveness of the internal controls and their related impact on the previously reported material weakness(es)
4. Discuss, with the engagement team, the results of the tests performed and the conclusions reached
5. Read the related report(s) to be issued
6. Evaluate sufficiency of documentation, as appropriate
7. Concurring approval of issuance of the report

We support a quality review, tailored to the related service or reporting being performed, for all PCAOB engagements.

Objective of the Standard

Question 2 – *Is the objective in the reproposed standard appropriately formulated? Does it articulate the purpose of an EQR?*

Question 3 – *Will this objective contribute to a more thoughtful and effective EQR?*

In our initial letter of comment, we supported the idea that an overall objective would be of significant benefit to ensure that the EQR achieves its intended result. We believe the proposal adequately articulates the purpose and overall role of the EQR and that the objective will contribute to a more thoughtful and effective EQR.

Qualifications of the Engagement Quality Reviewer

Question 4 – *Is it appropriate to explicitly require a reviewer from within the firm to be a partner or an individual in an equivalent position?*

Question 5 – *Should the standard allow qualified accountants who are not employed by an accounting firm to conduct the review?*

Question 6 – *Should the standard prohibit the engagement partner from serving as the reviewer for a period of time following his or her last year as the engagement partner? If so, is two years sufficient, or should it be extended?*

We believe a reviewer should have a strong background in accounting and auditing that can be supplemented by available literature and consultation with experts in specialized industries. In addition, it is important that the reviewer be of a similar level of authority as the engagement partner as it relates to matters affecting the conduct of the audit or review. We believe that it is more important to describe the characteristics of the reviewer and the expectation as to the level of authority required for audit matters rather than to specifically state that the individual must be a partner of a firm or “in an equivalent position.” There are many types of legal structures of accounting firms and even more differences in the design of how firms operationally structure their audit departments to ensure audit quality. At issue is how to make sure that qualified people perform the EQR role and that these qualified individuals are of sufficient authority within the firm issuing the report to be effective in eliminating audit deficiencies before the report is issued.

Therefore, we do not believe that explicitly stating that the EQR must be performed by a partner or “another individual in an equivalent position in the firm” is appropriate. Given the diversity of legal structure and operational design described in the paragraph above, we believe that there will be varying interpretations of what is meant by “an equivalent position.” For example, it is possible that the use of the phrase “an equivalent position” of a partner could be interpreted to be someone with the same authority in matters relating to the firm as a whole (as opposed to matters related to the conduct of audits and reviews) and this interpretation would preclude certain otherwise qualified individuals from performing the EQR in some firm structures simply because they did not have the authority a “partner” would have in the firm (e.g., ability to vote on partnership matters, ability to bind the firm to legal agreements, etc.). While we acknowledge that, in many structures, the level of experience and authority necessary to conduct an EQR will rest with individuals who hold the title of “partner” (or their equivalents in other types of legal structures such as shareholders in a professional corporation such as our firm), we do not believe that this is always required in order to develop an effective EQR. Consider a firm that chooses to establish a separate quality control department staffed with highly technical and experienced auditors and with sufficient authority over audit matters such that the firm cannot issue a report without the quality control department’s approval. Consider further that, for business and economic reasons, the firm may not choose to make these individuals “partners” of the firm nor an equivalent of a partner. In our view, the issue centers around having the appropriate level of authority within a firm’s structure to ensure that the EQR is in a position to provide the necessary experience and technical competence as well as to provide an effective independent review of the work performed by the engagement team. If a firm provides the appropriate authority to this quality control department, the fact that the individuals are not partners or the equivalent of partners (e.g., shareholders in a professional corporation, etc.) should not preclude such a structure from being used to meet the PCAOB’s objectives. An explicit statement of who can perform the EQR will potentially limit certain firms (and in particular, smaller firms or firms who centralize their quality review function) from meeting the spirit of the PCAOB’s intent in creating this standard.

We also believe that individuals outside the firm should be available to firms to accomplish the EQR function. This is especially important with smaller firms where there are a limited number of personnel employed by the firm with the appropriate expertise. In order to create a competitive environment and level playing field among providers of audit services, there needs to be an ability for firms to use qualified accountants to perform the EQR regardless of whether they are employed by the firm. We also see a potential ancillary issue in smaller firms where the number of personnel with a particular industry or subject matter expertise is limited. We recognize the PCAOB's view, as stated in the release, that in order to perform an effective EQR where industry expertise is important for the engagement team to have, so too should the EQR have similar expertise. We believe that smaller firms could be challenged to a detrimental degree if there is confusion about what is meant by the EQR (and anyone working on behalf of the EQR) being "independent" when performing their review. Consider the example where the engagement team consults on an issue with its national office (or in our case, Professional Standards Group). Can the EQR consult with the same people in the national office as the engagement team consulted or must the EQR use separate and independent industry and subject matter experts to evaluate the engagement team's conclusion? Our contention is that the Professional Standards Group personnel (or national office) are not members of the engagement team and therefore are available to both the engagement team and EQR as being "independent." Would the PCAOB agree with this assertion? If so, we believe that this nuance is not readily apparent in the definitions of independent in Item 6 "Independent, Integrity and Objectivity" of the release and should be clarified.

Lastly, we believe that it is necessary for the engagement partner to refrain from acting as the EQR for a period of time following their last year as the engagement partner. Currently, the rules require that the engagement partner and concurring reviewer must rotate off the engagement for a period of 5 years. The new proposal suggests that a 2 year period would be sufficient. We believe that the number of years is somewhat arbitrary but it should be substantive enough such that a new engagement team can exercise judgments that are free from the influence of the prior engagement team to avoid a continuation of potential bias toward decisions made in previous periods. As a result, this time period must, at a minimum, be more than one year and we believe that a 2 year period would be sufficient to allow the new engagement team to offer a fresh, objective look at the client.

EQR Process

Question 7 – *Are the descriptions of the scope and extent of the EQR procedures contained in the reproposed standard appropriate? Will the performance of these procedures result in a high-quality EQR? If not, how should these procedures be revised?*

Question 8 – *Are the specifically required procedures appropriately tailored to reflect the difference in scope between an audit and an interim review?*

Question 9 – *Do the specifically required procedures sufficiently focus the reviewer on areas of highest risk? Are there other areas that should be required?*

Office of the Secretary
PCAOB
April 21, 2009
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We believe that the procedures, as proposed, will result in a high quality EQR and that they are appropriately tailored to address areas of high risk and to meet the different needs of an audit and an interim review.

Concurring Approval of Issuance

Question 10 – *Is the standard for the engagement quality reviewer's concurring approval of issuance appropriately described in the reposed standard? Is the first condition appropriately tailored to reflect the difference in scope between an audit and an interim review?*

We believe that the standard appropriately describes the concurring approval.

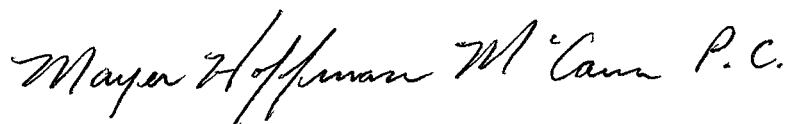
Documentation of the EQR

Question 11 – *Are the documentation requirements in the reposed standard appropriate? If not, how should they be changed?*

We believe the documentation requirements are reasonable.

If you have any questions regarding our comments, please contact Rich Howard, Regional Attest Practice Leader – West region at (949) 450-4402 or Ernie Baugh, National Director of Professional Standards at (423) 870-0511.

Very truly yours,

A handwritten signature in cursive script that reads "Mayer Hoffman McCann P.C.".

Mayer Hoffman McCann P.C.



Paris La Defense, April 20, 2009

Public Company Accounting Oversight Board

Office of the Secretary

1666 K Street, N.W.

Washington, DC 20006, USA

Attention: J. Gordon Seymour, Secretary, and the Members of the Board

Re: PCAOB Rulemaking Docket Matter No. 025 - Mazars comments on PCAOB proposed Auditing Standard on Engagement Quality Review - PCAOB Release No. 2009-001 March 4, 2009

Dear Sirs,

Mazars is a unique integrated partnership of European origin, specialized in audit, accounting, tax and advisory services. It assembles more than 10,500 professionals operating in 50 countries, led by more than 560 partners, and there are 12 additional countries where Mazars is present through correspondents and joint ventures (see Mazars annual report and its IFRS joint-audited consolidated financial statements on <http://www.mazars.com>). Moreover, via the Praxity Alliance of which Mazars is a founding member, Mazars can access the skills and expertise of a further 13,800 professionals in another 23 countries, all of whom possess a common desire to adhere to strong quality guidelines and a collective determination to exceed technical and ethical standards.

In North America, Mazars has a long standing presence via Mazars USA (created in 1988/1989, and registered with the PCAOB). As a natural extension of its development strategy, Mazars formed several joint ventures with members of Moores Rowland International (MRI) since 2000 to assist its clients in various corners of the world. At the end of 2006, Mazars and the American members of MRI, 5 well known US firms, decided to optimize their relationship, and signed an agreement to launch a new international alliance between independent structures, named Praxity, an international non-profit association registered in Belgium, which became operational in 2007.

As at 31 December 2008, Praxity had 109 participating firms in 72 countries, with more than 24,800 personnel and an aggregated fee income of US\$ 3.2 billion (Euro € 2.3 billion), including Mazars Group. Praxity is the world's largest alliance of independent accounting firms and is ranked in 8th position overall (International Accounting Bulletin's survey of Networks and Associations).

We want to preface our comments with general consideration that we fully support implementation of rules strengthening the audit quality, and the contribution of these rules to restore the public confidence in financial reporting and in the world's capital markets. Mazars is therefore fully committed to support PCAOB initiative, as well as those of IFAC, European Commission and other key European or national regulators or oversight that have been already doing good work and are implementing stronger controls in these areas of common concern.



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We are pleased to submit this letter in response to the PCAOB's invitation to comment on its proposed Auditing Standard on Engagement Quality Review.

We respectfully submit our detailed comments below. We commend the Board for the transparency of its rule deliberation process.

Q1 Page 8: Should the standard require an EQR for other kinds of engagements performed according to PCAOB standards? If so, what types of engagements should be included and what should an EQR of such engagements entail?

The original PCAOB's proposal required an EQR for all engagements performed in conformity with the PCAOB standards. These engagements included: integrated audits, audits of financials statements only, interim reviews, and other audit and attestation engagements. Some of the comments received questioned the practicality of applying the same EQR standards on engagements such as those referenced above that are very distinctive in nature. Based on this feedback, the PCAOB has now limited the scope of its re-proposed EQR standards to audit and interim review engagements. The issue raised here is to determine whether this re-proposed EQR standard should also be applicable to other kinds of engagements performed under PCAOB guidance.

Mazars subscribes to the idea that the standard should require an EQR for other kinds of engagements performed according to PCAOB standards. Mazars believes that the EQR standards should be crafted in such a way that they could be applicable on other PCAOB engagement-types such as attestations and reviews.

For instance, initially, the PCAOB developed AS 5¹ to be applicable to large corporations. Then, the PCAOB staff subsequently provided direction to auditors on scaling the audit based on the company's size and complexity. The new staff guidance² published on January 23, 2009, explains how auditors can apply the principles in AS 5 to audits of smaller, less complex public companies. Another example is COSO which originally issued guidance on Internal Control³ in 1992. This guidance provided principles-based guidance for designing and implementing effective internal controls. It established a common definition of internal control that services the needs of different parties for assessing and improving their control systems. Subsequently, COSO issued other guidance⁴ in 2006 geared towards smaller public companies.

Mazars believes that the PCAOB could use the same approach as shown in the two examples above.

¹ Auditing Standard No. 5, An Audit of Internal Control Over Financial Reporting That Is Integrated with An Audit of Financial Statements ("Auditing Standard No. 5")

² Staff Views – An Audit of Internal Control Over Financial Reporting That Is Integrated with An Audit of Financial Statements: Guidance for Auditors of Smaller Public Companies.

³ COSO - Internal Control — Integrated Framework (1992)

⁴ COSO - Internal Control over Financial Reporting — Guidance for Smaller Public Companies (2006)



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The PCAOB could develop one set of EQR standards (full framework) that are scalable and applicable to all types of PCAOB engagements (audit, review, and attest services). These EQR standards should be principles-based, cost-effective, risk-based, and customizable for application on all types of PCAOB engagements.

Q2 Page 9: Is the objective in the re-proposed standard appropriately formulated? Does it articulate the purpose of an EQR?

Mazars believes that the objective in the re-proposed EQR standard as currently stated could be simplified and broken down into two pieces for clarity purposes:

“The objective of the engagement quality reviewer is to perform an evaluation of the significant judgments made by the engagement team and the conclusions reached in forming the overall conclusion on the engagement and in preparing the engagement report, if a report is to be issued, in order to determine whether to provide concurring approval of issuance.”

The simplified objectives of the engagement quality reviewer would be as follows:

- 1) To perform an evaluation of the significant judgments made by the engagement team and the conclusions reached in forming the overall conclusion on the engagement and in preparing the engagement report, if a report is to be issued; and
- 2) To determine whether to provide concurring approval of issuance.

Mazars supports the inclusion of an objective evaluation provision in the re-proposed EQR standard to determine whether the stated EQR objective was met.

Q3 Page 9: Will this objective contribute to a more thoughtful and effective EQR?

In our May 12, 2008 comment letter on the original proposed EQR standard (page #3), we urged the PCAOB to seek rapprochement with the IAASB in developing EQR standards and future auditing standards. This consultation is in progress. On February 27, 2009, the IAASB announced that it has completed its Clarity Project⁵ which was started in 2004 as a comprehensive program to enhance the clarity of its International Standards on Auditing (ISAs). Thirty-six ISA standards in all were revised or restated.

The improvements derived from the Clarity Project broadly consisted of the following:

- 1) Identifying the auditor’s overall objectives when conducting an audit in accordance with ISAs;
- 2) Setting an objective in each ISA and establishing the auditor’s obligation in relation to that objective;

⁵ A complete history of the Clarity Project can be found at Clarity Center on the IAASB website www.ifac.org/IAASB



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- 3) Clarifying the obligations imposed on auditors by the requirements of the ISAs and the language used to communicate such requirements;
- 4) Eliminating any possible ambiguity about the requirements an auditor needs to fulfill; and
- 5) Improving the overall readability and understandability of the ISAs through structural and drafting improvements

As shown above, the first two benefits of the Clarity Project relate to the objectives of the ISA standards from the auditor's perspectives. Mazars believes as the IAASB does that a clearly stated objective is beneficial to the auditor because it leads to a more effective and efficient EQR process. A clearly formulated objective in the re-proposed EQR as shown above could lead to a more structured and thoughtful audit process.

Q4 Page 15: Is it appropriate to explicitly require a reviewer from within the firm to be a partner or an individual in an equivalent position?

Mazars believes that it is appropriate to explicitly require a reviewer from within the firm to be a partner or an individual in an equivalent position. This can serve several purposes:

- a) Meet a firm's quality control requirement (ISQC 1);
- b) Expose a partner or an individual in an equivalent position to new types of engagements (shared knowledge);
- c) Facilitate partners' rotation requirements (independence issue);
- d) Serve as training ground for young and promising partners;
- e) Serve as a performance evaluation tool for partners.

The level of partner or equivalent partner position is the one that assumes competence, qualification, and authority, which are all variables attached to an effective reviewer.

Q5 Page 15: Should the standard allow qualified accountants who are not employed by an accounting firm to conduct the review?

In Mazars' opinion, this proposed EQR standard should not allow qualified accountants who are not employed by an accounting firm to conduct the review. Allowing external qualified accountants to perform EQR could hamper the existing independence rules (mandatory rotation of engagement partners and independent reviewers) and increase the EQR monetary and administrative costs. It may also limit the potential growth of partners for whom the EQR is used as a learning ground or stepping stone for gaining industry knowledge. It may also pose certain risks to firms' quality control systems to bring in outsiders who lack the culture and values shared by firms' employees.



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However, Mazars would welcome any PCAOB's quality control program that would allow qualified accountants who are not employed by an accounting firm to conduct a peer-review of the quality control programs of firms. This would help the firms in their quest for continuing improvement.

Q6 Page 15: Should the standard prohibit the engagement partner from serving as the reviewer for a period of time following his or her last year as the engagement partner? If so, is two years sufficient, or should it be extended?

Mazars agrees with the idea that there should be a "cooling-off" period from the time an engagement partner completes his/her required rotation on an audit or interim review engagement and the time when he/she can resume any EQR activity on the same audit engagement.

We believe that a "cooling-off" period of 2 years, in-between an audit engagement and an EQR engagement, is adequate and reasonable. This proposal is also consistent with ISA 290.154(b)⁶ that recommends a 2-year lapsing period for audit engagement partners and EQ reviewers who have completed their normal rotation requirements of 7 years to resume any audit work on the same audit client.

Q7 Page 20: Are the descriptions of the scope and extent of EQR procedures contained in the re-proposed standard appropriate?

In general, the descriptions of the scope and extent of EQR procedures as re-proposed here appear adequate. Serious efforts were made in rewriting the proposals so as to allow the EQ reviewer to perform a thorough review or take a second look at the audit or interim review engagement without it appearing as a re-audit or a second interim review. There is a continuing focus on the audit and interim review greatest risks, on evaluating significant judgments made and conclusion reached by engagement team, and on evaluating engagement documentation.

Will the performance of these procedures result in a high-quality EQR? If not, how should these procedures be revised?

We believe that in general, the performance of these procedures could result in a high-caliber EQR. However, we would like the Board to consider other factors that may impact the EQR process such as:

- a) Joint-audits – There is a trend towards joint-audits in Asian countries, and joint-audits are also called for public or financial sector audits, or in some exceptional cases, such a recent fraud case in India, where two firms were engaged to re-audit the company investigated for fraud;
- b) Evaluation of supervision, review, and approval process during audit engagements;
- c) The proportionality of EQR review time versus the actual audit or interim review time.

⁶ IFAC Code of Ethics § 290



The PCAOB itself in its recent inspection report⁷ (page 20) raised (b) and (c) issues as follows:

... “Certain deficiencies raised questions about the sufficiency, rigor, and effectiveness of the supervision and review activities of engagement managers and partners, including the thoroughness with which they reviewed audit documentation. In some cases, it appeared that the engagement partners had not devoted sufficient attention to their responsibilities, or their commitment to engagements did not appear to correlate with the risk that the engagements presented. Certain of the deficiencies described above were in areas that required management’s most difficult or complex judgments, and thus were in areas where the partners and managers should be devoting significant attention”...

“In addition, some of the deficiencies were in areas that ordinarily would be reviewed by the concurring review partner. Further, in some instances, the inspection teams observed that the concurring review partner for an audit for which there were deficiencies committed a relatively small amount of time, compared to the firm’s overall commitment to the audit. These observations suggest that there may have been weaknesses in the applicable firm’s policies and procedures, or the application of them, in this important area”....

Q8 Page 20: Are the specifically required procedures appropriately tailored to reflect the difference in scope between an audit and an interim review?

We believe that the specifically required procedures are appropriately tailored to reflect the difference in scope between an audit and an interim review.

Q9 Page 20: Do the specifically required procedures sufficiently focus the reviewer on areas of highest risk? Are there other procedures that should be required?

Mazars believes that the specifically required procedures adequately focus the reviewer on areas of highest risk. However, Mazars would like to encourage the PCAOB to find ways to supplement these proposed procedures with certain specific and limited procedures that touch upon some of the most challenging audit areas covering:

- a) Auditing fair value measurements
- b) Auditing accounting estimates
- c) Auditing the adequacy of disclosures
- d) Auditor’s consideration of a company’s ability to continue as a going concern, etc

⁷ Report on the PCAOB’s 2004, 2005, 2006, and 2007 Inspections of Domestic Annually Inspected Firms / PCAOB Release 2008-008 December 5, 2008

http://www.pcaobus.org/Inspections/Other/2008/12-05_Release_2008-008.pdf



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The idea is to alert the EQ reviewer about challenging audit areas so that he/she must exercise extra EQR due diligence without it being considered re-audit or second review engagement. The current financial crisis has led several accounting and auditing standard-setters to publish alerts that provide directions to accountants and auditors on ways to treat certain subjects. The IAASB and the PCAOB could also issue alerts directed towards EQR issues.

Mazars would support clarifications of the terms “read”, “review”, and “evaluate” used throughout this re-proposed standard.

Q10 Page 24: Is the standard for the engagement quality reviewer’s concurring approval of issuance appropriately described in the re-proposed standard? Is the first condition appropriately tailored to reflect the difference in scope between an audit and an interim review?

Per the PCAOB, the reviewer “*may provide concurring approval of issuance only if, after performing with due professional care the review required by this standard, he or she is not aware of a significant engagement deficiency.*” A “*significant engagement deficiency*” is defined as any of these four conditions:

- 1) *The engagement team failed to obtain sufficient appropriate evidence in accordance with the standards of the PCAOB;*
- 2) *The engagement team reached an inappropriate overall conclusion on the subject matter of the engagement;*
- 3) *The engagement report is not appropriate in the circumstances; or*
- 4) *The firm is not independent of its client.*

Mazars believes that the standard for the engagement quality reviewer’s concurring approval of issuance as proposed is not appropriately described. We agree with the idea that the reviewer must perform his/her review with such degree of due professional care to be able to concur in the issuance of the audit report. However, it appears that in order to conclude that the first condition is possibly met, (1) *the engagement team failed to obtain sufficient appropriate evidence in accordance with the standards of the PCAOB*, the reviewer must perform a level of review of working papers that could be considered too close to a re-audit. Said differently, it appears that this condition, in order to pass the “muster test”, requires higher level of review procedures than those proposed above (scope and extent of review procedures).

We propose that the reviewer be required to explain and document the basis for arriving at any of his/her conclusions.



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Q11 Page 26: Are the documentation requirements in the re-proposed standard appropriate? If not, how should they be changed?

Mazars believes that the documentation requirements in the re-proposed standard are less specific than the original ones. The original proposal provided that the engagement documentation should indicate:

- 1) who performed the review;
- 2) the areas of the engagement subject to the review;
- 3) the procedures performed by the reviewer;
- 4) when the review procedures were performed;
- 5) the results of the review procedures; and
- 6) whether the engagement quality reviewer provided concurring approval of issuance.

The new proposal (on page 28) states that, the documentation should “contain sufficient information to identify”:

- 1) who performed the review;
- 2) the documents reviewed;
- 3) the significant discussions held during the review;
- 4) the date that the reviewer provided concurring approval of issuance; and
- 5) if the reviewer did not provide concurring approval of issuance, documentation of the reviewer's reasons for not providing concurring approval of issuance.

A line-by-line comparison between the original and the new proposal shows that the latter eliminated the old items # 3 and # 5 that call for indicating the EQR procedures performed and the results obtained. We do not see how removing these two items enhances the effectiveness of the EQR procedures. In fact, these two items clarify the EQR process.

Moreover, the new proposal leaves plenty of room to interpretations by referring to the concept of “sufficiency of information” as a threshold to assess the adequacy of documentation. This situation raises the issue of how to assess the reasonableness of the documentation from a qualitative and quantitative point of view. What scale does the reviewer use to evaluate his/her documentation? We all agree that the EQR shall be both risk-based and principles-based. However, at a minimum an effective EQR guidance should require disclosures by reviewers of the EQR procedures used and the results obtained.

Mazars agrees with the Board that:

- 1) the reviewer and the engagement team should determine the appropriate timing for the review procedures
- 2) the statement that the reviewer should complete his/her review before providing concurring approval of issuance is abundantly clear throughout the proposed EQR and no additional explicit statement is warranted



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Mazars also generally agrees with the Board in regard to the effective dates for implementing this re-proposed EQR standard. It appears that the start period proposed, subject to SEC approval, is reasonable:

- a) EQRs of interim reviews - fiscal years beginning after December 15, 2009
- b) EQRs of audits - fiscal years ending on or after December 15, 2009

We hope that our comments above will be helpful and we remain available for further considerations. Please feel free to contact us again if you would like to discuss our submission further.

Yours sincerely,

A handwritten signature in blue ink, appearing to read 'J. Barlet'.

Jean-Luc Barlet
Mazars
Risk Management & Audit Quality

McGladrey & Pullen

Certified Public Accountants

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Third Floor
3600 American Blvd West
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O 952.835.9930

April 20, 2009

J. Gordon Seymour, Secretary
Public Company Accounting Oversight Board
1666 K Street, N.W.
Washington, D.C. 20006-2803

RE: PCAOB Release No. 2009-001, Rulemaking Docket No. 025 – *Proposed Auditing Standard – Engagement Quality Review*

Dear Mr. Seymour:

McGladrey & Pullen, LLP is pleased to submit comments regarding the proposed auditing standard, *Engagement Quality Review*. McGladrey & Pullen, LLP is a registered public accounting firm serving middle-market issuers.

McGladrey & Pullen, LLP supports the issuance of an engagement quality review standard that more clearly articulates the standard of performing an engagement quality review. We believe the changes that were made to the original proposed standard more appropriately define the requirements of an engagement quality review. However, we also believe certain modifications should be made to the revised proposal to clarify various sections of the standard and enhance its application in practice.

Objective

We believe the objective set forth in the proposed standard should be revised to clarify that the evaluation of the significant judgments made by the engagement team and the conclusions reached in forming the overall conclusion on the engagement and in preparing the engagement report relate to the significant judgments identified through the performance of the procedures set forth in paragraphs 9 through 18 of the proposed standard. We suggest the following objective:

The objective of the engagement quality reviewer is to ~~perform an evaluation of~~ evaluate, through the performance of the engagement quality review procedures set forth in this standard, the significant judgments made by the engagement team ~~and the conclusions reached~~ in forming the overall conclusion on the engagement and in preparing the engagement report, if a report is to be issued, in order to determine whether to provide concurring approval of issuance.

Qualification of an Engagement Quality Reviewer

We do not support the prohibition set forth in paragraph 8 of the proposed standard, which prohibits the engagement partner for either of the prior two audits from performing the engagement quality review. As noted in the release, SEC independence rules limit an individual to five consecutive years of service as the engagement or concurring partner, but do not prohibit that individual from serving in either capacity during that five-year period. We also note that there would be no prohibition against the engagement quality reviewer subsequently serving as the engagement

partner within the same five-year period. We believe the fact that another individual would be serving as the engagement partner sufficiently mitigates any risk that the engagement quality reviewer would not challenge judgments made and conclusions reached in prior audits. In addition, we believe the current SEC rule provides for adequate protection against a loss of objectivity due to prolonged association with the audit client and this prohibition may impose a hardship on smaller registered public accounting firms.

Engagement Quality Review Process for an Audit

Paragraphs 9 and 10 prescribe general and specific requirements for conducting the engagement quality review of an audit. We generally agree with the types of procedures to be performed. However, we recommend certain changes in the text of paragraphs 9 and 10 to better align with the intentions of the Board as set out in the Release and the objective of the standard. In addition, we do not believe the language in paragraph 9 is sufficiently clear to communicate that engagement quality reviewers are able to complete the review by reviewing selected documentation. We note Paragraph 11 refers to "engagement documentation ...reviewed when performing the procedures required in paragraph 10." However, this same clarification is not articulated in paragraph 9. Accordingly, we recommend paragraph 9 be modified as follows:

In an audit engagement, the engagement quality reviewer should evaluate the significant judgments made by the engagement team ~~and the conclusions reached~~ in forming the overall conclusion on the engagement and in preparing the engagement report. To identify and evaluate the significant judgments ~~and conclusions~~, the engagement quality reviewer should perform the procedures described in paragraph 10 by holding discussions with the person with overall responsibility for the engagement, by holding discussions with other members of the engagement team as necessary, and by reviewing selected audit documentation.

Further, we suggest the following changes to certain steps in paragraph 10 which we believe are consistent with the guidance in paragraph 9 and will help clarify the process by which the engagement quality reviewer performs the review.

10. In an audit, the engagement quality reviewer should:

- a. Evaluate the significant judgments made in engagement planning, including –
 - The consideration of the firm's recent engagement experience with the company and risks identified in connection with the firm's client acceptance and retention process,
 - The consideration of the company's business, recent significant activities, and related financial reporting issues and risks, and
 - The judgments made about materiality and the effect of those judgments on the engagement strategy.
- b. Evaluate the risk assessments and audit responses, including the identification of significant risks, including significant fraud risks, and the engagement procedures performed in response to significant risks.
- d. Evaluate judgments made by the engagement team about (1) the materiality and disposition of corrected and uncorrected misstatements identified and aggregated by the engagement team and (2) the severity and disposition of identified control deficiencies.

Further, we believe the procedures set forth in paragraphs 10.e. and 10.f. which require the reviewer to “determine if appropriate matters have been communicated, or identified for communication” and “determine if appropriate consultations have taken place on difficult or contentious matters” could be interpreted to go beyond the other requirements of the standard that are focused on the evaluation of the work performed by the engagement team. We believe the procedures in paragraphs 10.e and 10.f. of the standard should be modified to indicate that the engagement quality reviewer should make an evaluation of the appropriateness of such matters based upon performing the procedures set forth in this standard.

We suggest these two paragraphs be modified as follows:

e. Determine if Evaluate whether appropriate matters that are identified through the performance of the engagement quality review have been communicated, or identified for communication to the audit committee, management, and other parties, such as regulatory bodies.

f. Determine if Evaluate whether appropriate consultations have taken place on difficult or contentious matters identified through the performance of the engagement quality review. Review the documentation, including conclusions, of such consultations.

Alternatively, the Board could include these two procedures in a new paragraph which would follow paragraph 10 and clarify that the evaluation should be made based upon the results of all other procedures performed in accordance with this standard.

Finally, we suggest the definition of “significant risk” as set forth in footnote 24 of the Release be added as a footnote to paragraph 10.b.

Documentation of an Engagement Quality Review

Paragraph 19.b. requires the engagement quality reviewer to identify the “documents” reviewed by the engagement quality reviewer and others who assisted the reviewer. We are unclear as to what is meant by “documents” and believe this paragraph should be clarified to state whether the requirement is to identify the areas of audit documentation reviewed by the engagement quality reviewer; agreements and contracts reviewed in connection with the performance of the review; or documents containing the financial statements as described in paragraph 10.h.

Paragraph 19.c. requires that documentation should include sufficient information to identify the significant discussions held by the engagement quality reviewer and others who assisted the reviewer, including the date of each discussion, the specific matters discussed, the substance of the discussion, and the participants. We believe the requirement is unnecessarily burdensome and will result in additional costs that are not likely to provide a commensurate benefit to audit quality. As a result, we recommend it be deleted.

The engagement team’s existing obligation to prepare documentation consistent with the objective and requirements of PCAOB Auditing Standard No. 3, *Audit Documentation*, when combined with the proposal’s requirement to indicate which documents were reviewed by the engagement quality reviewer and his or her assistants, should provide adequate documentation of the basis for the engagement quality reviewer’s compliance with the standard.

If the Board continues to believe it is necessary to document discussions involving the engagement quality reviewer, we recommend that paragraph 19 be revised to include the explanation of what constitutes a “significant discussion” as described in footnote 36 of the Release.

Effective Date

As proposed, the standard would be effective for audits of fiscal years ending on or after December 15, 2009, and for interim reviews for fiscal years beginning after December 15, 2009.


As it relates to audits, we believe the effective date should be linked to the beginning of an audit engagement period. By linking the effective date to the beginning rather than the end of an audit engagement period, the new requirements would (1) be known and anticipated as of the beginning of the audit engagement period by auditors, audit committees and companies, (2) allow the assigned engagement quality reviewer to comply with the requirements throughout audit engagement planning and execution, and (3) apply equally to each interim review during an audit period to which the proposed standard applies.

Due to the anticipated timing of final approval of the standard by the SEC, we are also concerned the proposed effective dates would not permit sufficient time for registered public accounting firms to effectively and efficiently implement the new EQR requirements. As proposed, we believe implementation might require significant changes to a firm's quality control processes, particularly those firms that have not historically performed concurring reviews. The effective date should provide all registered public accounting firms with sufficient time to (1) adopt policies and procedures consistent with the new standard, (2) train their personnel in the requirements of the new standard, and (3) assign or engage qualified engagement quality reviewers consistent with their system of quality control.

Accordingly, assuming the SEC approves the final standard not later than September 30, 2009, we believe the PCAOB should base the effective date on fiscal year periods beginning after December 15, 2009, to provide adequate time for firms to prepare for adoption. If SEC approval does not occur prior to September 30, 2009, we believe the standard should not become effective until quarterly and annual periods beginning after December 15, 2010.

Thank you for the opportunity to comment on this proposed standard. Please direct any questions concerning our comments to Bruce Webb, Executive Partner – National Office of Audit and Accounting (515.281.9240) or Scott Pohlman, SEC Coordinator (952.921.7734).

Sincerely,



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April 17, 2009

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

Via e-mail: comments@pcaobus.org

Re: Request for Public Comment: *Proposed Auditing Standard – Engagement Quality Review, PCAOB Rulemaking Docket Matter No. 25*

Dear Office of the Secretary:

We appreciate the opportunity to share our views on the Public Company Accounting Oversight Board's (PCAOB or the Board) Proposed Auditing Standard on *Engagement Quality Review*, and Conforming Amendment to the Board's Interim Quality Control Standards (the proposal or proposed standard).

We would like to take this opportunity to recognize the significant effort of the Board and its staff in developing the proposed standard. We believe a well performed engagement quality review enhances audit quality. We further believe that extending the requirement to other firms that previously were not members of the AICPA's SEC Practice Section is an appropriate step to ensure consistent quality control standards for audits of public companies.

We also appreciate the PCAOB's willingness to expose a revised proposal. In comparing the proposed standard with the initial proposal we support the changes made by the PCAOB, most notably to (1) clarify that applicability is limited to audit engagements and engagements to review interim financial information, (2) add an objective to enable the engagement quality reviewer to better assess when he or she has fulfilled the objective and (3) eliminate from the proposal the requirement for the reviewer to affirmatively conclude that there is nothing he or she "knows or should know" in order to provide concurring approval of issuance. While we generally support these and other changes made by the Board, we believe further changes are necessary to clarify the Board's intent and to enable us to effectively implement the proposed standard. Our comments and recommendations are provided in the remainder of this letter.

Objective of the Engagement Quality Reviewer

As noted above, we support the addition of an objective to the proposal. However, we believe the objective would be improved if it clarified that an evaluation of the conclusions reached are those that relate to the significant judgments in an engagement. We do not believe the Board intended that



Office of the Secretary
Public Company Accounting Oversight Board
April 17, 2009
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the engagement quality reviewer review *all* of the conclusions reached during an engagement. Accordingly, we recommend paragraph 2 be revised to clarify that the objective is meant to indicate a review of the “...*significant judgments made by the engagement team and the related conclusions reached...*”.

Engagement Quality Review Process

We believe the proposal does not put appropriate limits on the extent of the activities of an engagement quality reviewer. We recommend that the Board clarify that the engagement quality reviewer uses his or her professional judgment when performing the role, in the context of due professional care. We believe such a change will enhance engagement quality, promoting the focus of the engagement quality reviewer on the significant judgments and related conclusions made by the engagement team. In this regard, we believe further clarifications in paragraphs 9 and 10 are necessary.

For example, paragraph 9 of the proposal requires that, “*to identify and evaluate the significant judgments and [related] conclusions, the engagement quality reviewer should perform the procedures described in paragraph 10 by holding discussions...and by reviewing documentation.*” We believe these requirements, as written, are too open-ended. In this light, we believe it important that the Board clarify that the engagement quality reviewer need not review all file documentation or hold discussions with all engagement team members, but that he or she complete these procedures based on his or her professional judgment. The open-endedness of these procedures is especially concerning given the Board’s statement on page 24 of the proposal’s release that “*the requirement to exercise due professional care imposes on a reviewer essentially the same requirement as the ‘knows, or should know based on the requirements of this standard’ formulation in the Board’s original proposal,*” as we further comment below.

Accordingly, we believe that the engagement quality reviewer should review *selected* documentation that he or she believes is necessary to perform the role. Additionally, we believe that the engagement quality reviewer should hold discussions with other personnel involved in the engagement, including members of the engagement team or personnel involved in consultations, when, based on his or her professional judgment, he or she believes it is necessary. We recommend the following revisions to paragraph 9:

In an audit engagement, the engagement quality reviewer should evaluate the significant judgments made by the engagement team and the related conclusions reached in forming an overall conclusion on the engagement and in preparing the engagement report. To identify and evaluate the significant judgments made by the engagement team and related conclusions, the engagement quality reviewer should perform the procedures described in paragraph 10 by holding discussion with the person with overall responsibility for the engagement, by holding discussions with other members of the engagement team and other personnel involved in any significant consultations as considered necessary by the engagement quality reviewer, and by reviewing selected documentation as considered necessary by the engagement quality reviewer.

We also suggest conforming changes to paragraph 14 of the proposal with those noted above.

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Also, we believe the procedures listed in paragraphs 10.e. and 10.f. (for audits) and paragraph 15.b. (which incorporates the requirements of paragraphs 10.e. and 10.f.) (for interim reviews) of the proposal could be interpreted by an engagement quality reviewer to require separate stand alone “determinations” rather than an evaluation of the significant judgments and related conclusions reached by the engagement team. We strongly recommend that paragraphs 10.e. and 10.f. of the proposal be modified to clearly indicate that the procedures noted therein are to include an evaluation of the information learned through the performance of the other engagement quality review procedures in the standard.

Furthermore, we believe certain aspects of paragraphs 10.a., 10.b. and 10.d. (for audits) and paragraphs 15.a. and 15.b. (which incorporates the requirements of paragraph 10.d.) (for interim reviews) of the proposal could be interpreted by an engagement quality reviewer to require a detailed review in contrast to focusing on the significant judgments and related conclusions reached by the engagement team. We suggest the Board modify these paragraphs to clarify that these procedures are intended to apply to significant judgments made by the engagement team. We believe that this change, in combination with the changes to paragraphs 9 and 14 suggested above allowing the engagement quality reviewer to review selected documentation necessary to fulfill his or her responsibility, will result in the appropriate level of involvement of the engagement quality reviewer.

Concurring Approval of Issuance

We observe that paragraphs 12 and 17 of the proposal indicate “*the engagement quality reviewer may provide concurring approval of issuance only if, after performing with due professional care the review required by this standard, he or she is not aware of a significant engagement deficiency.*”

We support the negative form of assurance and the requirement to exercise due professional care in performance of the role, both of which concepts are consistent with the Board’s interim standards. We believe the requirement to conduct the engagement quality review with due professional care is an improvement over the legalistic “knows or should know” standard of the original proposal. However, we are concerned by and disagree with the Board’s comments in its release on page 24, wherein the Board suggests that “*the requirement to exercise due professional care imposes on a reviewer essentially the same requirement as the ‘knows, or should know based on the requirements of this standard’ formulation in the Board’s original proposal.*” We are not aware of precedent that would cause the standard of due professional care to be an equivalent to the Board’s previously proposed “knows or should know” standard. If precedent exists or if the Board is attempting to redefine due professional care, we ask that the Board provide additional clarification, and to propose a re-definition of the term in the Board’s interim standard AU Section 230, *Due Professional Care in the Performance of Work*. Otherwise, we believe this constitutes a significant conflict between the proposal and the proposal’s release, and between the proposal’s release and existing auditing standards, that should be resolved by the Board in its final standard to prevent unnecessary concern and confusion when performing an engagement quality review.

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Documentation of an Engagement Quality Review

We believe the requirement in paragraph 19(c), which would require documentation of “*significant discussions held by the engagement quality reviewer and others who assisted the reviewer, including the date of each discussion, the specific matters discussed, the substance of the discussion, and the participants,*” is overly prescriptive, cumbersome and burdensome to the engagement process. Consequently, we recommend that the Board remove the requirement in paragraph 19(c) from the proposed standard.

The engagement quality reviewer has frequent discussions with members of the engagement team during the course of an engagement. It is unreasonable to expect that an engagement quality reviewer would be able to determine which discussions would qualify as “significant discussions” on a real time basis without the benefit of hindsight and without transcribing each discussion. As such, this requirement would necessitate documenting the details of each discussion with other members of the engagement team and therefore, result in significant time, effort and cost. We believe the costs of attempting to comply with this detailed requirement would significantly outweigh any of the intended benefits.

It is also unclear to us how this documentation requirement would serve to improve engagement quality. The additional time and costs to be incurred when attempting to comply with the details of this requirement may have the unintended consequence of creating barriers to the timing and frequency of discussions between the engagement quality reviewer and engagement team during the course of an engagement. Further, the engagement team is required to prepare audit documentation in accordance with PCAOB Auditing Standard No. 3, *Audit Documentation*. This documentation should be a sufficient basis for demonstrating the engagement quality reviewer’s compliance with the proposed standard, which should include the significant judgments and related conclusions reached by the engagement team during an engagement. If in forming an overall conclusion the engagement quality reviewer believes that the engagement documentation does not support the significant judgments and related conclusions reached during an engagement, he or she should not provide his or her concurrence until such documentation is included or appropriately modified as required by paragraph 16 of the proposal. Accordingly, we believe requiring additional documentation of discussions with the members of the engagement team is unnecessarily redundant and does not improve engagement quality.

Effective Date of the Proposed Standard

We believe that the proposed effective date for audits of fiscal years ending on or after December 15, 2009, will not permit sufficient lead time to implement the proposed standard in an efficient and effective manner. A final standard is not likely to be adopted until well into calendar year 2009. By that time, auditors will have completed a significant amount of work on annual audit engagements. The changed responsibilities of the engagement quality reviewer would be effective for work already performed or underway. We believe implementing this change well into an audit cycle will cause inefficiencies and might detract from the effectiveness of interim reviews during that period. In this regard, we believe that the effective date of the proposed standard should be linked to the beginning of an audit engagement period. An effective date that is linked to the beginning of an audit period, rather than the end, will allow us to adhere to the new requirements during the entire audit engagement period, including each interim review within the period.

Office of the Secretary
Public Company Accounting Oversight Board
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Convergence with Other Standards Setters

Similar to the recommendations made in our letter dated February 18, 2009, to the Board on its proposed risk assessment standards, we continue to encourage the Board to leverage as much as possible from existing standards adopted by the International Auditing and Assurance Standards Board (IAASB). We suggest the Board use the International Standards on Auditing (ISAs) as a common base for current and future standards-setting, modifying them as it sees fits for a public company audit. We believe a higher degree of convergence will lead to higher quality and more efficient audits.

In a firm our size or smaller, the public company audit practice often represents a smaller part of the firm's client base, and as such the audit approach for the entire firm is not strictly designed around PCAOB standards. It is difficult for a firm and practitioners to incorporate into their audit approach multiple sets of standards that vary from each other either slightly or completely, without a full understanding of the reasoning for the differences. In this regard, we believe it would be helpful if the Board included a comparison between the ISAs and its engagement quality review proposal to assist firms with effective and efficient implementation.

PCAOB's Standard Structure

Firm quality control - We observe the proposed *auditing* standard includes presumptively mandatory requirements related to a registered firm's system of quality control in the note to paragraph 4. We believe it is preferable for the Board to include requirements for registered public accounting firms in quality control standards and to only include auditor requirements in the auditing standards.

Structure of the Board's standards - We see a lack of consistency in how definitions are presented in the proposal. Definitions are included in the proposal's release and in "Notes" included in the proposal. This lack of consistency makes it more difficult to know how to interpret the proposed standard. For example, it is not clear to us if definitions included in the proposal's release are intended to be authoritative. We believe all definitions, if intended to be authoritative, should be included in the auditing standard, and in a consistent manner. We also find the use of "Notes" confusing. We do not understand why the Board is using "Notes" instead of including the text within a paragraph of the proposal. We recommend the Board discontinue the use of "Notes" or provide additional clarification why the proposal includes "Notes" and how we are to interpret and apply the "Notes". In this light, we believe the Board would benefit by implementing standards of organization and structure for use in its auditing standards, such as that recently implemented by the IAASB in its Clarity Project.

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Public Company Accounting Oversight Board
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* * * * *

We would be pleased to discuss our comments with members of the Public Company Accounting Oversight Board or its staff. If you have any questions, please contact Jeff Brown, Director of Assurance Services (206-302-6814) or Fred Frank in our Professional Practice Group (206-302-6915).

Very truly yours,

Moss Adams LLP



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April 20, 2009

J. Gordon Seymour, Office of the Secretary
Public Company Accounting Oversight Board
1666 K Street, N.W.
Washington, D.C. 20006-2803

By e-mail: comments@pcaobus.org

**Re: PCAOB Release No. 2009-001 –
Proposed Auditing Standard, *Engagement Quality Review*
(PCAOB Rulemaking Docket Matter No. 025)**

Dear Mr. Seymour:

The New York State Society of Certified Public Accountants, representing 30,000 CPAs in public practice, industry, government and education, welcomes the opportunity to comment on the above captioned release.

The NYSSCPA's Auditing Standards Committee deliberated the release and prepared the attached comments. If you would like additional discussion with us, please contact Robert N. Waxman, Chair of the Auditing Standards Committee at (212) 755-3400, or Ernest J. Markezin, NYSSCPA staff, at (212) 719-8303.

Sincerely,



Sharon Sabba Fierstein
President

Attachment



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**NEW YORK STATE SOCIETY OF
CERTIFIED PUBLIC ACCOUNTANTS**

**PCAOB Release No. 2009-001
COMMENTS ON PROPOSED AUDITING STANDARD – ENGAGEMENT
QUALITY REVIEW
(PCAOB Rulemaking Docket Matter No. 025)**

April 20, 2009

Principal Drafters

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**New York State Society of Certified Public Accountants
Auditing Standards Committee**

**Comments on
PCAOB Release No. 2009-001
Comments on Proposed Auditing Standard - Engagement Quality Review**

The New York State Society of Certified Public Accountants welcomes the opportunity to comment on the PCAOB's Proposed Auditing Standard - *Engagement Quality Review*. Responses to specific questions in the proposal follow:

Question 1. Should the standard require an EQR for other kinds of engagements performed according to PCAOB standards? If so, what types of engagements should be included and what should an EQR of such engagements entail?

We believe this standard, aimed at audits and interim reviews, appropriately excludes the other types of engagements mentioned in the proposal, those being (a) the attestation required under Item 1122 of Regulation AB regarding the company's compliance with its servicing criteria, or (b) an AS 4 ("Reporting on Whether a Previously Reported Material Weakness Continues to Exist") attestation regarding material weaknesses.

Question 2. Is the objective in the repropoed standard appropriately formulated? Does it articulate the purpose of an EQR?

We believe the objective in paragraph 2 is appropriate.

Question 3. Will this objective contribute to a more thoughtful and effective EQR?

Yes. This auditing standard places the burden of concurrence on the EQ Reviewer who, of necessity, would have to weigh the various judgments made by the audit or review team and therefore be more thoughtful. Our answer assumes the question whether the EQ Review will be "more thoughtful and effective" was meant to address whether this proposal will be more effective than the current concurring partner review requirements.

Question 4. Is it appropriate to explicitly require a reviewer from within the firm to be a partner or an individual in an equivalent position?

We support the requirement that the reviewer be a partner or its equivalent in the firm. We recommend that "an individual in an equivalent position" be specifically defined in the final Standard.

Question 5. Should the standard allow qualified accountants who are not employed by an accounting firm to conduct the review?

Yes, we agree that qualified accountants, who under paragraph 3 must be an associated person of a registered public accounting firm, should be allowed to conduct reviews.

Question 6. Should the standard prohibit the engagement partner from serving as the reviewer for a period of time following his or her last year as the engagement partner? If so, is two years sufficient, or should it be extended?

We believe that two years is sufficient and should not be extended, and that the exception for firms with less than five issuers and less than ten partners (in Rule 2-01(c)(6)(ii) of Regulation S-X) be considered in the final standard.

Question 7. Are the descriptions of the scope and extent of EQR procedures contained in the repropoed standard appropriate? Will the performance of these procedures result in a high-quality EQR? If not, how should these procedures be revised?

We agree with the scope and extent of the listed procedures.

Question 8. Are the specifically required procedures appropriately tailored to reflect the difference in scope between an audit and an interim review?

We believe that the differences in procedures to be performed by the EQR in an audit and in an interim review, as proposed, appropriately reflect the differences between the two types of engagements.

Question 9. Do the specifically required procedures sufficiently focus the reviewer on areas of highest risk? Are there other procedures that should be required?

We agree the specifically required procedures will help focus the EQ Reviewer on those areas of highest risk and offer no other required procedures.

See Additional Comment below on page 3.

Question 10. Is the standard for the engagement quality reviewer's concurring approval of issuance appropriately described in the repropoed standard?

Yes.

Question 10 (cont.). Is the first condition appropriately tailored to reflect the difference in scope between an audit and an interim review?

Yes.

Additional Comment regarding Paragraph 19:

In that the EQR must date and document the concurring approval (or lack of approval) of issuance (paragraph 19(d)), the extensive documentation requirement leading up to that approval (in paragraph 19(c)) is unnecessary and goes beyond the objective of the standard (paragraph 2). We see no need to document in detail every significant discussion by the EQR and by others who may have assisted the reviewer.



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April 20, 2009

Reply to Fergus Falls office
Direct: 218-998-7106

Mr. J. Gordon Seymour
Secretary
Public Company Accounting Oversight Board
1666 K Street, N.W.
Washington, DC 20006-2803

RE: PCAOB Rulemaking Docket Matter No. 025 – Engagement Quality Review

Dear Mr. Seymour:

The purpose of this letter is to provide comments from Otter Tail Corporation on the Public Company Accounting Oversight Board's Proposed Auditing Standard – Engagement Quality Review. Otter Tail Corporation had revenues of \$1.3 billion in 2008. Established in 1907 as an electric utility, Otter Tail has expanded its scope to include interests in health services, manufacturing, plastics, food ingredient processing, construction and transportation. Our audit fees, exclusive of non-recurring items and non-audit services have approximated \$1.3 million. It is important to us to manage our costs and the annual audit fees are a cost that we monitor closely. Any regulatory rulemaking proposal that potentially affects the aggregate costs of audit services is of interest to us.

We appreciate the work the Board has put into this proposed standard in order to strengthen the existing requirements and process for an Engagement Quality Review (EQR) and lead to consistency in the application of a standard for EQRs. After reviewing the Proposed Standard we feel that some of the provisions could lead to duplication and we have concerns with the amount of time that might be spent on the EQR. These processes could lead to increased audit fees to companies such as Otter Tail. For your consideration we provide the following comments.

Paragraphs 12 and 17 – Concurring Approval of Issuance

We agree with the Board's requirement that the EQR be conducted with due professional care. Due professional care is a concept familiar to auditors and consistent with other auditing standards. We are however concerned with the language on page 24 of the Release that the "requirement to exercise due professional care imposes on a reviewer essentially the same requirement as the "knows, or should know" based on the requirements of this standard". It is very difficult to determine what "should know" is. "Should know" is more easily determined after the fact than during the actual process. We would not want the reviewer doing the same amount of work as the engagement partner. We would recommend removal of the relationship of due professional care to "knows, or should know".

Paragraph 19 – Documentation of an Engagement Quality Review

Paragraph 19(c) requires that the documentation of the EQR include significant discussions held by the reviewer and others who assisted the reviewer, including the date of each discussion, the specific matters discussed, the substance of the discussion and the participants. Our concern here would be with potential redundancy of documentation within the audit workpapers. We are concerned with the amount of time that will be spent by the reviewer in preparing this documentation. Similar documentation of the discussions between the engagement partner and the reviewer may have also been made within the audit workpapers. It may be determined by the reviewers that they need to document each discussion in order to comply with this Proposed Standard. That would seem to be overly burdensome to the audit firm and costly to the firm's clients.

Thank you for this opportunity to provide comments to this Proposed Standard. Our primary concern is that the Board find a way to balance meeting the objectives of the EQR without significant cost increases to the companies being audited.

Sincerely,

A handwritten signature in cursive script that reads "Debra Wilke".

Debra Wilke
Director, Corporate Accounting

PIERCY BOWLER TAYLOR & KERN

Certified Public Accountants • Business Advisors

April 13, 2009

To: Office of the Secretary
Public Company Accounting Oversight Board
1666 K Street, N.W.
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Transmitted by e-mail to: comments@pcaobus.org

Re: PCAOB Rulemaking Docket Matter No. 025 — Engagement Quality Review

As we did in our letter of April 28, 2008, in response to the Board's Release 2008-002 (the first Release), we are pleased to respond again in this letter to its revised proposal contained in Release 2009-001 (the second Release) regarding engagement quality reviews (referred to as EQRs), previously termed "concurring partner reviews." As noted in our earlier response, we understand the Board's concerns about the consistency from firm to firm and from engagement to engagement of the application of a standard for EQRs and the ability of the Board's inspectors to evaluate the scope of a given review in relation to such a standard.

We appreciate and respect the Board's apparent responsiveness to the 38 letters of comment it received with regard to the first Release and its decision to expose a revised proposal for comment. We regret to note, however, that it appears from some of the explanatory discussion in the second Release that some of the issues may have been preliminarily resolved for reproposal purposes based more on the weight of the number of respondents favoring one position over another rather than the relative merit of the alternative views expressed and considered.

Except for our general observations in the paragraph immediately following we have included all of our concerns, observations and comments, with some overlap, in our numbered responses to the questions posed by the Board in the second Release. These are identified as **Q1-Q11** in our detailed responses on the pages that follow the executive summary of our key positions on pages 2-3, which we have prepared for the convenience of the Board and the staff. Our most critical concerns are set forth under **Q1, Q4, Q6 and Q8-Q11**.

As we observed in our response to the first Release, we believe there is useful guidance contained outside the body of the current proposed standard that should be incorporated into either the body of the final standard itself or in the footnotes thereto. For example, certain guidance and definitions are contained only in footnotes 24, 28, 36 to the second Release rather than to the proposed standard. Also, we would like to convey that, unlike several commentators to the first Release, we do not support the notion that the Board should allow itself to be influenced to conform to, or converge with, international standards and should remain steadfast in its leadership.

Thank you for this opportunity to comment. We hope the Board finds our comments useful in its deliberations on this important matter.

Very truly yours,



Howard B. Levy, Sr. Principal and Director of Technical Services
Piercy Bowler Taylor & Kern, Certified Public Accountants

Below is a classified summary of the key positions of our firm on the issues upon which the Board requested comments. For the convenience of the Board and other readers, these summary position statements are also included on the following pages in boldface type preceding our detailed comments made in response to the specific questions raised in the second Release, which detailed responses also contain support for these positions.

A. Applicability of the EQR Requirement

- The EQR requirements should apply only to audits, as prescribed by Congress, and not to reviews primarily because they would likely lead to excessive user reliance on the review process in relation to the scope of the underlying work.

B. Objective of the Standard

- The core of the stated objective should more closely track Rule 2-01(f)(7)(ii)(B) of Regulation S-X, supplemented by interpretive language explaining the basis, nature and limitations of the additional assurance provided and clearly distinguishing the reviewer's responsibilities and those of the engagement partner.
- The objective should be accompanied by clear statements that it does not contemplate either (a) a review of all judgments and work of others (and excludes any original substantive work by the reviewer), or (b) an assessment of the design or degree of compliance with the firm's quality controls.

C. Qualifications of the Engagement Quality Reviewer

- We would agree with the proposed qualifications if (a) the terms "partner" and "equivalent position" were expressly linked in the standard to the definition of "audit partner" in Rule 2-01(f)(7)(ii) of Regulation S-X, and (b) it were made clear that those terms refer to the nature of responsibilities and not to equity ownership.
- We believe the standard should acknowledge that authority should be a consideration in assigning reviewers but state that it should rarely be a problem if the firm has an appropriate disagreement policy and tone-at-the-top.
- We object to the statement on pp. 7-8 of the second Release that "the Board believes that application of this requirement would rarely, if ever, allow a manager or other non-partner in an accounting firm to perform the EQR" because we believe this reference to "other non-partner" has an extremely high potential of inappropriately biasing the judgments of PCAOB inspectors, other regulators and triers of fact. We believe the statement should be expressly withdrawn with an explanation.
- The standard should include qualitative and quantitative criteria as to recent audit experience in addition to "associated person" status for reviewers from outside the audit firm.
- The standard should not expand upon the current rotation requirements by prohibiting an engagement partner who has not served his or her allotted five years from serving as a reviewer for two years after his/her last service as an engagement partner.

D. EQR Process

- Except for some relatively minor editorial suggestions, the proposed scope requirements for audits appear adequate.

- An EQR should not be required for a review, but if it were to be required, the proposed scope and concurring approval for issuance would be excessive.

E. Concurring Approval of Issuance

- It appears, but is not clear, that the Board intends that a positive approval be issued for audits based on negative assurance. Sample wording for such an approval should be provided in the standard.
- The statements made in the second Release and accompanying materials equating the “due professional care” formulation with the previously proposed “knows or should know” formulation is erroneous and poses litigation risks to auditors. It should be expressly withdrawn.
- A concurring approval for issuance should not be required for a review.

F. Documentation of the EQR

- The proposed requirements of paragraph 19b and c are excessive. We generally prefer the documentation proposal in the first Release, subject to certain modifications, most significantly, to eliminate the proposed vague requirement to document the “results.”

SEE DETAILED COMMENTS BEGINNING ON PAGE 4.

A. Applicability of the EQR Requirement

- **The EQR requirements should apply only to audits, as prescribed by Congress, and not to reviews primarily because they would likely lead to excessive user reliance on the review process in relation to the scope of the underlying work.**

Q1 — *Should the standard require an EQR for other kinds of engagements performed according to PCAOB standards? If so, what types of engagements should be included and what should an EQR of such engagements entail?*

From the way the question is framed, it appears that the Board is interested only if commentators believe the proposal in the second Release should be expanded beyond what is proposed to other types of services performed under PCAOB standards. It remains our view, however, as we set forth in our April 28, 2008, letter in response to the first Release, that the proposed requirement should not be expanded from what it is in the SECPS §1000.08(f) and §1000.39 (Appendix E, item d) of the PCAOB's Interim Quality Control Standards (IQCS). We mean it should be limited to audits (except to the extent it now applies to interim reviews, *i.e.*, a passive role for the reviewer to participate in timely discussions initiated by engagement team members about matters identified in the review that are perceived to involve a significant risk of material misstatement).

As noted in our response to the first Release, we understand that the stated objective of Section 103 of the Sarbanes-Oxley Act of 2002 (the Act) was for the PCAOB to include in its auditing standards a requirement for EQRs, that was to be applicable to all audits of issuers (as defined in the Act). We also share the Board's apparent view of the importance of the contribution to audit quality that such a standard can and should make. We recognize that Section 103(a)(2)(A)(ii) of the Act is the only statutory reference therein to an EQR (albeit by its previous name) and note, however, that by its language (as acknowledged by the Board in footnote 26 to the second Release), the requirement for an EQR is limited in its applicability only to audits (the vague parenthetical expression "and other related information" therein notwithstanding). Although the Board's authority to go beyond the minimum statutory requirements of Section 103(a)(2) is clearly set forth in Section 103(a)(3)(A)(i) of the Act and, therefore, not subject to question, we believe it is doubtful that Congress ever intended the ECQ requirement to be extended to interim reviews conducted pursuant to AU Sec. 722, "Interim Financial Information," of the PCAOB's Interim Auditing Standards (IAS). Accordingly we question the statutory basis and intent for the SEC's unexplained references in Rule 2-01(f)(7)(ii)(B) of Regulation S-X to the review service.

Moreover, we believe the following considerations make the Board's proposal to apply active EQR procedures to interim reviews to be inherently impractical and counterproductive:

- We reiterate (as also noted in our response to the first Release) that we do not believe the imposition of a mandatory, active EQR of any scope is warranted by the limited assurance provided or implied, or by the nature and extent of the procedures performed in support thereof, in an IAS AU Sec. 722 review. Accordingly, we believe that investment community knowledge of an expanded EQR requirement applicable to interim financial information will likely lead to widespread misunderstandings consisting of an exaggerated sense of reliability ascribed to such information that is considerably more than is reasonably warranted in relation to the limited scope of the underlying work currently prescribed pursuant IAS AU Sec. 722. (This point considers the fact that IAS AU Sec. 722 requires only analytical procedures and inquiries for a review service and does not, in any circumstances, require one to obtain any supporting evidence for client assertions, a condition not likely to be well-known by financial statement users because review reports are rarely included in filings.)
- We further believe that adding another level of review that necessarily requires significant time expenditure by a reviewer impair issuers' ability to cope with the additional constraints for timely

reporting applicable to interim financial reporting (especially for accelerated filers) with no measurable improvement to the reliability of such reporting.

Accordingly, as set forth in the first paragraph, above, we continue to believe that the EQR requirement for interim reviews should remain limited as it now is to a passive responsibility to participate in timely discussions initiated by engagement team members about matters identified in the review that are perceived to involve a significant risk of material misstatement. We believe such limitation on the EQR requirement to be consistent with the limited scope of the review service, reasonable investor expectations based thereon and the time constraints inherent in interim reporting; therefore, it is the only practical choice.

B. Objective of the Standard

- **The core of the stated objective should more closely track Rule 2-01(f)(7)(ii)(B) of Regulation S-X, supplemented by interpretive language explaining the basis, nature and limitations of the additional assurance provided and clearly distinguishing the reviewer’s responsibilities and those of the engagement partner.**
- **The objective should be accompanied by clear statements that it does not contemplate either (a) a review of all judgments and work of others (and excludes any original substantive work by the reviewer), or (b) an assessment of the design or degree of compliance with the firm’s quality controls.**

Q2 — *Is the objective in the reposed standard appropriately formulated? Does it articulate the purpose of an EQR?*

We fail to see the benefit to be achieved from stating the objective as that of the reviewer rather than of the EQR, itself, the latter of which we believe is more appropriate (although both alternatives should be virtually the same and, therefore, inseparable). We disagree with the Board’s expressed belief that framing the objective as one of the reviewer effectively emphasizes “the responsibilities placed on a reviewer by this proposed standard,” nor do we believe that such emphasis is needed. Moreover, the proposed objective, as framed in paragraph 2 of the current proposed standard, appears merely to be an extremely brief and overly mechanical summary of the procedures to be employed and conclusions to be reached and, as written, does not add anything useful or meaningful to the proposed standard.

We frankly believe the core and essence of an explicit statement of objective of the review, of which we are absolutely in favor, should be broader, less procedural and more qualitative than that proposed by more closely tracking the language embodied in Rule 2-01(f)(7)(ii)(B) of Regulation S-X (excluding the references to reviews), with suggested qualifying additional language shown in bold italics, *i.e.*, “to provide additional assurance that the financial statements subject to the audit ... are in conformity with generally accepted accounting principles and the audit ... and any associated report are, ***in all significant respects***, in accordance with ... auditing standards and rules promulgated by the Commission or the Public Company Accounting Oversight Board.” This core statement should be supplemented with proximate interpretive language in the body of the standard (rather than in an accompanying release) as discussed below in our response to **Q3**.

Q3 — *Will this objective contribute to a more thoughtful and effective EQR?*

To be clearer, and to enable a more rigorous or robust, thoughtful and effective EQR, we believe the core statement of objective suggested in our response to **Q2**, above, should be supplemented with interpretive language in the body of the standard explaining briefly but more specifically what should be the basis and nature of the added assurance to be afforded by the EQR, possibly combining words such as those used in IQCS SECPS §1000.39 with those contained in paragraph 20 of Redrafted ISA 220, with suggested qualifying additional language shown in bold italics, *e.g.*, “...an objective evaluation, ***in accordance with the***

applicable standard of the PCAOB, of significant auditing, accounting, and financial reporting judgments made by the engagement team and the conclusions reached in formulating the audit report.”

Additionally, we believe the portion of the final standard containing the stated objective should also articulate the key limitations of the EQR process. For example, the body of the final standard should clearly state, in close proximity to the objective now in paragraph 2, that:

- The term “additional assurance,” as used in Rule 2-01(f)(7)(ii)(B), does not mean absolute assurance.
- The EQR “reviewer’s responsibility is not the equivalent of the engagement partner’s responsibilities” (as is now stated in IQCS SECPS §1000.39, paragraph b).
- The reviewer’s participation does not relieve the primary engagement partner or equivalent from the final responsibility for issuing the firm’s report(s).

(This notion is more or less effectively carried over from the IQCS to the current proposed standard in paragraph 7, which reads “[t]he person who has overall responsibility for the engagement remains responsible for the engagement and its performance, notwithstanding the involvement of the engagement quality reviewer,” but should be relocated to reside in the discussion of the objective of the EQR.)

- The objective calls for a review of only the significant, but not all, judgments and work of others and does not call for any original substantive work by the reviewer, and lastly,
- The objective does not contemplate that the EQR is shall be intended for the purpose of assessing the design or degree of compliance with the firm’s quality controls (although it may result in the identification of needs for improvement therein).

C. Qualifications of the Engagement Quality Reviewer

- **We would agree with the proposed qualifications if (a) the terms “partner” and “equivalent position” were expressly linked in the standard to the definition of “audit partner” in Rule 2-01(f)(7)(ii) of Regulation S-X, and (b) it were made clear that those terms refer to the nature of responsibilities and not to equity ownership.**
- **We believe the standard should acknowledge that authority should be a consideration in assigning reviewers but state that it should rarely be a problem if the firm has an appropriate disagreement policy and tone-at-the-top.**
- **We object to the statement on pp. 7-8 of the second Release that “the Board believes that application of this requirement would rarely, if ever, allow a manager or other non-partner in an accounting firm to perform the EQR” because we believe this reference to “other non-partner” has an extremely high potential of inappropriately biasing the judgments of PCAOB inspectors, other regulators and triers of fact. We believe the statement should be expressly withdrawn with an explanation.**
- **The standard should include qualitative and quantitative criteria as to recent audit experience in addition to “associated person” status for reviewers from outside the audit firm.**
- **The standard should not expand upon the current rotation requirements by prohibiting an engagement partner who has not served his or her allotted five years from serving as a reviewer for two years after his/her last service as an engagement partner.**

Q4 — *Is it appropriate to explicitly require a reviewer from within the firm to be a partner or an individual in an equivalent position?*

Our answer to **Q4** depends on what is intended to be meant by the terms “partner” and “equivalent position.” As we noted in our response to the first Release, the SEC’s Rule 2-01(f)(7)(ii) of Regulation S-X does not require or even suggest that an audit partner, including one described in Rule 2-01(f)(7)(ii)(B) who performs an EQR in accordance with PCAOB rules, needs to have any equity ownership in the firm to function effectively in such “partner” role. (This fact is acknowledged in footnote 15 to the second Release, which reads “...but they do not prohibit non-partners from performing that function” but which is too far removed from the standard, itself.) We believe a clear statement that equity ownership is not required should appear in the body of the final standard, rather than in accompanying release, along with definitions of “partner” and “equivalent position” that are consistent with Rule 2-01 (f)(7)(ii) of Regulation S-X but more specific with respect to EQR reviewers.

In defining such “partner” roles and setting forth their qualifications, Rule 2-01 rightfully speaks only to the nature of responsibilities. We believe that the SEC position as stated in Rule 2-01(f)(7)(ii) essentially already requires that a reviewer be in an equivalent position as that of an audit partner, but only as defined therein (without regard to equity ownership), and that to require equity ownership is both unnecessary and unduly burdensome on smaller firms that do not have the depth of resources at the equity partner level of the larger firms.

We note that there are no professional standards that define the qualifications of an engagement partner. Such qualifications and assessments of competence are left to the professional judgment of individual firms to determine and are subject to periodic critical evaluation by PCAOB inspectors. In that regard, we believe the allocation of equity interests in a firm is often solely an economic decision that has (and should have) little or nothing to do with, and is an independent consideration from, those involved in assigning responsibilities or authority and evaluating professional competence. We believe that a reasonably robust standard for qualifying EQR reviewers will serve an effective quality control over the selection of both engagement partners and reviewers without any dependency on their status as equity-holding partners. This should be made clear in the final standard.

By way of example, as the PCAOB was made aware in connection with our two inspections, our firm (like many similarly small firms, we believe) is structured with both shareholders and nonequity-holding principals, the latter of whom are judged upon their promotion to such status to have sufficient experience and professional competence to enable them to function effectively at the “partner” level, as described in Rule 2-01(f)(7)(ii) of Regulation S-X, on many engagements for both issuers and nonissuers alike. These nonequity-holding principals and shareholders are all subjected to another evaluation of their competence and experience at the engagement principal level, and are both held to the same standard, before being assigned to perform an EQR.

We, therefore, believe that if the final standard were to explicitly require a reviewer from within the firm to be a “partner or an individual in an equivalent position,” the term “partner” should be explicitly defined in the standard by reference to the definition of “audit partner” in Rule 2-01(f)(7)(ii), and the term “equivalent position” should be expressly limited by a definition that refers only to responsibilities (as it is in Rule 2-01 (f)(7)(ii)) and, perhaps, authority, which is closely related. Moreover, it should be more clearly and directly articulated in the body of (or a footnote to) the standard that equity ownership is neither a requirement of the standard, nor should it be viewed necessarily as evidence of competence.

While we agree with the Board’s statement in the second Release that “what constitutes authority is not easily defined,” we firmly hold the view that a precise definition is not necessary in a standard but rather, the standard should state clearly that the firm’s management is responsible for assuring that the reviewer has the appropriate level of authority to meet effectively the objectives set forth in the standard for performing an EQR. Like many

other requirements of many other standards, such determinations should be left to the judgment of management of the individual registered firms, subject to periodic evaluation by PCAOB inspectors.

We believe that it is inherently fallacious logic to conclude (as the Board seems to have done in the second Release) that “concerns about authority will most often arise when the reviewer is employed by the same firm as the engagement partner.” We believe the contrary is more likely true. However, when the firm has, as part of its quality control structure, both a well-drafted and effective policy for resolving professional disagreements (pursuant to IAS AU Sec. 311.14) and an appropriate “tone-at-the-top” (note that §1000.39 states, “The tone set at the top of the firm should encourage and support the performance of objective concurring partner reviews”), there should never be any significant issues with authority in connection with an EQR, whether the reviewer comes from the same firm or not. We also believe that the substance of the foregoing sentence should be articulated in the body of or a footnote to the final standard.

Accordingly, we firmly object to the statement on pp. 7-8 of the second Release that “the Board believes that application of this requirement would rarely, if ever, allow a manager or other non-partner in an accounting firm to perform the EQR” because we believe the reference to “other non-partner” has an extremely high potential of inappropriately biasing the judgments of PCAOB inspectors, other regulators and triers of fact. Accordingly, we believe it is neither necessary nor appropriate for any standard, or the release accompanying the standard upon issuance, to contain such potentially prejudicial language. The facts and circumstance should be independently judged on their own in each case. Accordingly, we hope such prejudicial language will be expressly withdrawn, along with an appropriate explanation of the reason for such withdrawal, in the release that will accompany the final standard. We further believe that, to remove any doubts in this regard, the standard should explicitly state that a competent manager may serve as an assistant to the EQR reviewer, for example, to provide needed industry expertise, since the authority of the principal EQR reviewer will be attributed to all assistants.

Q5 — *Should the standard allow qualified accountants who are not employed by an accounting firm to conduct the review?*

If the question is intended to refer only to accountants not employed by the reporting firm, as it seems to be, our answer is yes. As stated in our response to **Q4**, above, we believe that when the firm has an adequate policy for resolving professional disagreements and an appropriate “tone-at-the-top” as part of its quality control structure, there should never be an issue with authority in connection with an EQR whether the reviewer comes from the same firm or not. Accordingly, provided the reviewer meets the proposed requirements relative to competence, independence, integrity and objectivity, with which we fully concur, we believe such individuals should be permitted to conduct EQRs.

If the question is intended to refer to accountants not employed by any accounting firm, our answer would be no. However, the language in paragraph 3 of the proposed standard requiring the reviewer to be “an associated person of a registered public accounting firm” (as that term is defined in PCAOB Rule 1001(p)(i)) would serve effectively to eliminate most accountants from consideration who are not currently engaged in accounting practice such as a professor, a retired partner or an accountant in industry. Nevertheless, there is somewhat contradictory language in the last paragraph of the discussion of competence on p. 8 of the second Release that suggests, without qualification, that EQR reviewers may, in fact, be professors or retired partners. Accordingly, we believe this contradictory language should be expressly withdrawn in the release accompanying the final standard. But considerably more significant in our opinion, is the fact that there is no assurance that even an “associated person,” in fact, will be directly or indirectly involved in audit practice.

Accordingly, we believe the term “associated person of a registered public accounting firm” is far too broad to serve as a sufficiently selective criterion because we believe it is generally impossible for a person to meet the general competence standard and be “qualified” unless his or her experience in financial auditing meets both qualitative and quantitative criteria. Therefore, we believe that, in addition to the currently proposed

“associated person” criterion, the final standard should be expanded to require a currency of audit experience threshold (such as within the most recent year) and a definition of qualifying audit experience expressed in terms of activities. This is recommended, of course, because the challenges of modern financial auditing are too quickly growing and otherwise changing to permit someone with outdated experience to perform this critical quality control function.

Q6 — *Should the standard prohibit the engagement partner from serving as the reviewer for a period of time following his or her last year as the engagement partner? If so, is two years sufficient, or should it be extended?*

While we understand that the perceived benefit of the two-year “cooling off” period contained in paragraph 8 of the current proposed standard to be the “fresh look” objectivity of the reviewer for his or her first EQR (and we recognize that this requirement was a provision of the old standard embodied in paragraph a of IQCS SECPS §1000.39 but effectively superseded by the current rotation rules set forth in Rule 2-01(c)(6) of Regulation S-X), we firmly believe that such accelerated rotation would be unnecessary and in many cases would reduce audit quality. Our belief is based on the view that the benefit of familiarity with the client’s business and industry that one gains from experience on an audit far outweighs the potential benefit of a “fresh look” for purposes of meeting the objectives of an EQR, including assuring the appropriate level of audit quality. We believe it is likely that the SEC staff wisely considered the relative weight of these offsetting benefits when it drafted the current rotation rules that do not require any “partner” rotation after less than five years on the audit, regardless of the partner’s function.

We wish to point out further in this regard that it is common in practice to assign the engagement partner and reviewer in the same initial year (*i.e.*, when a new engagement is obtained) and thus face a need to rotate them both off the engagement concurrently five years later. We believe the sacrificing of experience and familiarity with the client caused by such a concurrent rotation severely reduces audit quality. By rotating the reviewer off and re-assigning the engagement partner to conduct the EQR in the fifth instead of the sixth year, the “fresh look” objective is met a year before it is actually required under present rules by the assignment of a new engagement partner, and this enables the staggering of mandatory rotations by one year thus avoiding the concurrent rotation of both the engagement partner and reviewer and the necessary consequential reduction in audit quality. Although this staggering could be achieved by larger firms without reassigning a new engagement partner to conduct the EQR in the fifth year, the proposed change in the rotation requirements would create a substantial burden for smaller firms that do not have the depth of resources in the number of qualified reviewers available and, we believe, result in a net loss, rather than a gain, in audit quality.

D. EQR Process

- **Except for some relatively minor editorial suggestions, the proposed scope requirements for audits appear adequate.**
- **An EQR should not be required for a review, but if it were to be required, the proposed scope and concurring approval for issuance would be excessive.**

Q7 — *Are the descriptions of the scope and extent of EQR procedures contained in the repropoed standard appropriate? Will the performance of these procedures result in a high-quality EQR? If not, how should these procedures be revised?*

Except as noted in the following paragraph, we believe that the nature and extent of ECQ procedures proposed to be employed for audits are both appropriate and appropriately described in paragraphs 9, 10 and 11 of the current proposed standard and, therefore, that they would likely result in a high quality EQR, given the competence, integrity and independence of the reviewer that should be reasonably assured by the operation of the standard and the firm’s tone-at-the-top. Nevertheless, we believe this section of the final

standard should emphasize the need for the reviewer to exercise objective professional judgment as to the scope of the review procedures necessary to meet his or her EQR responsibility.

We have the following suggestions for improving paragraph 10 of the current proposed standard.

- Notably missing from paragraph 10 is any specific requirement to inspect and evaluate the documentation of the audit work supporting judgments and conclusions expressed or implied about significant risk areas of the audit for compliance with applicable PCAOB auditing standards. If this is to be implied from what is in paragraph 10, we believe it is too subtle.
- We believe the requirements of both subparagraphs e and f of paragraph 10 are too sweeping and should be expressly limited to the significant matters otherwise subjected to EQR attention. They also should be characterized as subjective “evaluations” or “assessments” rather than absolute “determinations.”
- Lastly, contrary to the view of the CAQ as expressed in its May 12, 2008, comment letter to the first Release, we believe it would be appropriate to add a subparagraph c to paragraph 11 that would call for evaluation of compliance with the requirements of AS No. 3 and any applicable documentation provisions of other standards, which evaluation, like subparagraphs a and b, would be limited to those areas subjected to review under paragraph 10.

In contrast to our support of the proposed requirements to be applicable to audits, however, we have serious reservations about the nature, extent and descriptions of ECQ procedures, if any, to be required, such as are proposed in paragraphs 14-16 for use in interim reviews and have set forth our reservations in our response to **Q1**, above and **Q8**, below.

Q8 — *Are the specifically required procedures appropriately tailored to reflect the difference in scope between an audit and an interim review?*

Based on the reasons set forth in our response to **Q1**, above (consisting principally of the lack of apparent evidence of Congressional intent to extend the EQR requirement to interim reviews, the low level of service provided and of assurance afforded, whether provided or implied, by an IAS AU Sec. 722 review, and the time constraints inherent in interim reporting, the last two of which make the Board’s proposal impractical), we believe no EQR should be required for reviews. If an EQR were to be required, however, for the same reasons, we believe the general scope and specific procedures contained in paragraphs 14-16 (including those contained in paragraphs 10c-f that are incorporated by reference), and the concurring approval for issuance conclusion described in paragraph 17, of the current proposed standard for an interim review would be far in excess of what is warranted under the circumstances.

Q9 — *Do the specifically required procedures sufficiently focus the reviewer on areas of highest risk? Are there other procedures that should be required?*

Subject to our comments under **Q7**, above, we believe the specific procedures described in paragraph 10 of the current proposed standard do, in fact, sufficiently focus the reviewer on areas of highest risk in most circumstances, and we believe paragraph 10 needs to be supplemented only by cautionary language reminding reviewers to exercise objective judgment in determining scope.

E. Concurring Approval of Issuance

- **It appears, but is not clear, that the Board intends that a positive approval be issued for audits based on negative assurance. Sample wording for such an approval should be provided in the standard.**

- **The statements made in the second Release and accompanying materials equating the “due professional care” formulation with the previously proposed “knows or should know” formulation is erroneous and poses litigation risks to auditors. It should be expressly withdrawn.**
- **A concurring approval for issuance should not be required for a review.**

Q10 — *Is the standard for the engagement quality reviewer's concurring approval of issuance appropriately described in the repropoed standard? Is the first condition appropriately tailored to reflect the difference in scope between an audit and an interim review?*

Particularly in view of its controversial developmental history in this regard, we believe the standard is notably deficient by its omission of an illustrative example suggesting how one might word the required concurring approval of issuance for an audit. Most significantly, it is not clear from the words either in the second Release or the current proposed standard, itself (as it was in the first Release and accompanying proposed standard), if the Board still wishes to preclude the use of negative assurance. It appears (but is also not clear) from the language in paragraph 12 of the current proposed standard that it would be acceptable for a positive approval for issuance to be based on a form of negative assurance, *i.e.*, that, based on having performed the EQR with due professional care in accordance with the applicable PCAOB standard, the reviewer “is not aware of a significant engagement deficiency.” As we have illustrated, we think the language used to support a concurring approval for issuance should be based on an assertion by the reviewer of compliance with the PCAOB standard for performance of an EQR, which should either state or imply and be understood to include the exercise of due professional care. We think this needs to be clarified.

Since we do not believe an EQR or a concurring approval of issuance should be required at all for an interim review, we refer you to our response to **Q8**, above.

Moreover, we believe the release that will accompany the final standard should contain language that explicitly withdraws statements made in and accompanying the second Release expressing the view that references to “due professional care” that were substituted for the “legalese” and objectionable, “knows or should know” language contained in the earlier proposal, in substance, means the same thing. In our opinion, and we believe most likely those of others who commented on the earlier proposal, it does not, and to allow such a suggestion to remain uncorrected on the public record could have the same damaging effect on practitioners in future litigation that was perceived by such commentators (including us) as would be if the objectionable language were to be left in the standard, itself.

F. Documentation of the EQR

- **The proposed requirements of paragraph 19b and c are excessive. We generally prefer the documentation proposal in the first Release, subject to certain modifications, most significantly, to eliminate the proposed vague requirement to document the “results.”**

Q11 — *Are the documentation requirements in the repropoed standard appropriate? If not, how should they be changed?*

We note that in various places (including most explicitly in paragraph 7 of the current proposed standard), the Board acknowledges that the overall responsibility for the engagement and its performance, would still rest with the engagement partner, not the EQR reviewer. Yet, with regard to documentation requirements (particularly those set forth in paragraph 19b and c), the proposed standard appears to ignore this principle since they go substantially beyond those of PCAOB AS No. 3 and other standards that apply to the responsibilities of the engagement partner and other team members. The proposed requirements of paragraph 19b and c include making a record of the documents reviewed and documenting significant discussions held

during the review, “including the date of each discussion, the specific matters discussed, the substance of the discussion, and the participants.” Specifically, our concerns are:

- The overriding sense one gets in reading paragraph 19b is that it will require a more intense and rigorous review of identified documents than may be warranted in any given circumstances, thus virtually eliminating any room for professional judgment as to degree of attention a reviewer needs give to the review of any specific documents (and the extent of documentation necessary or appropriate). We believe this will have the likely unintended effect of elevating the related responsibility of an EQR reviewer to a higher level than that of the engagement partner in direct contrast to the cited statement in paragraph 7. We believe the proposed requirement in paragraph 19b to identify the documents reviewed is too prescriptive and has no match in present standards applicable to an engagement partner.
- Apparently since the engagement partner’s responsibility is for the overall engagement, there is no requirement in AS No. 3 or elsewhere in the currently applicable standards to match the proposed requirement in paragraph 19b for an engagement partner to identify all the documents reviewed. Paragraph 6b of AS No. 3 effectively requires that of the person taking specific responsibility for performing and reviewing the work (no mention of whether this should be the partner) done on a particular document. Ordinarily, an engagement partner will take the reviewer’s responsibility under AS No. 3, paragraph 6b, when no other reviewer on the audit team is qualified to or has done so. Nevertheless, the engagement partner will apply some level of review to many significant documents without taking express responsibility as a reviewer by signing off on the document.
- To require specific identification of documents examined would be tantamount to requiring the reviewer to take express responsibility for the document. In general, to enable the engagement partner to take such express responsibility for reviewing specific documents, he or she can be expected to feel obligated to spend more time than might otherwise be warranted on it, for example, checking cross-references and mathematical computations. Such would be generally true for the EQR reviewer as well, thus adding substantial duplicative and, therefore, unnecessary time and costs to the audit and considerably slowing down the public release of audited financial information.
- Notably most troublesome to consider about the proposed requirement of paragraph 19b is the also unintended likely effect that such a requirement might, in fact, serve as disincentive for a reviewer to inspect one or more documents that he or she otherwise might or should, thus reducing the quality of the EQR.
- We likewise believe that the proposed requirements of paragraph 19c regarding “significant discussions” go far beyond any requirement that now applies under current standards to the engagement partner or any other member of the audit team and are, in our opinion, costly, inefficient and quite excessive. Moreover, it appears that compliance would add nothing to the quality of either the audit or the EQR and would serve no useful purpose other than to facilitate criticism of the EQR reviewer by potential adversaries, for example, as to the identification of what were, in fact, “significant discussions” requiring documentation or as to the content and quality of such documentation.

We believe these requirements will often have the effect of setting the reviewer up as a “straw man” to be readily blamed in any future adversary proceeding relating to the quality of the audit to a greater extent than the engagement partner merely because of the relative ease of asserting noncompliance with a written standard.

Accordingly, we strongly prefer, in general, the documentation proposal in the first Release, which was primarily to document the broad audit areas of the engagement subjected to the EQR, but as we stated in our response to the first release, only if the final standard (a) makes it clear that the requirement proposed in paragraph 14c of the earlier proposed standard were intended to call for only broad, general descriptions of the procedures employed by the reviewer, such as the descriptions contained in paragraphs 8-10 of the earlier

proposed standard, and not specifically by area or in the level of detail ordinarily expected for audit programs and other audit documentation, and (b) that the proposed requirement to document specific “results” of such procedures be removed because:

- It is inherently vague and seems tantamount to requiring the retention of review notes (an inherently unwise practice), and
- We believe such a documentation trail to be of no value once a final concurring approval for issuance has been either granted or denied).
- For reasons set forth in the preceding paragraph, we do not believe it is either necessary or desirable to make the earlier proposal more prescriptive or “clearer” in any other respect.



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April 20, 2009

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

RE: PCAOB Rulemaking Docket Matter No. 025, *Proposed Auditing Standard - Engagement Quality Review*

Dear Sir:

PricewaterhouseCoopers LLP appreciates the opportunity to respond to the Public Company Accounting Oversight Board's (PCAOB or the "Board") Release No. 2009-001: *Proposed Auditing Standard - Engagement Quality Review* (the "standard" or "proposed standard").

We support the Board's continuing effort to promulgate auditing standards that promote audit quality. We believe that robust and effective engagement quality reviews that focus on the significant judgments made and related conclusions reached by the engagement team further that purpose. We commend the Board for its consideration of the constructive comments made by its constituents during the formal comment period, and for exposing a significantly improved second proposal which takes into account many of the comments received on the first proposal.

Some areas where we believe the second proposal improves upon the first include: (1) providing an objective of the engagement quality reviewer in the standard; (2) appropriately limiting the scope of the applicability of the standard to audits and interim reviews; (3) removing the proposed requirement that in addition to all of the other engagement quality review procedures, the engagement quality reviewer assess whether there are areas within the engagement that pose a higher risk that the engagement team has failed to obtain sufficient competent evidence or reached an inappropriate conclusion; (4) clarifying the procedures expected to be performed and documented by the engagement quality reviewer; and (5) changing the description of the basis of the overall conclusion.

We have provided suggestions in the remainder of our letter that we believe will address our remaining concerns and further improve the standard. Additionally, although we acknowledge the Board's decision to depart from the International Standards on Auditing (ISAs) in both the original and revised proposals, we maintain our view, as expressed in our February 18, 2009 comment letter in response to the PCAOB's proposed risk assessment standards, that the Board should consider using the ISAs as the base from which to develop its standards, as other national standard setters are doing, and add to or modify the ISA wording for requirements and guidance only as the Board deems necessary for audits, including integrated audits, of issuers.

Objective of Engagement Quality Reviewer

As noted above, we support the Board's inclusion of an objective for the proposed standard, which we believe appropriately focuses the engagement quality review on matters relevant to audit quality. The objective helps to clarify that the standard does not aim to create an additional level of independent



substantive auditing procedures nor does it require the engagement quality reviewer to engage in substantive oversight of the audit engagement team, substantively evaluate the performance of the engagement team, or determine compliance with the audit documentation requirements. The objective also recognizes that the responsibilities of the engagement quality reviewer, an element of a firm's quality control, differ from those of the engagement partner.

We recommend, however, that the Board make one clarifying edit to the objective by stating that the review relates to the "significant judgments made by the engagement team, and the related conclusions reached." We suggest that this same clarification be carried throughout the standard.

Engagement Quality Review Process for an Audit

Paragraphs 9 and 10 include procedures for conducting the engagement quality review of an audit. We agree with the changes in the revised proposal that clarify the extent of documentation that the engagement quality reviewer should review; however, we do not believe the language in paragraph 9 is sufficiently clear to communicate that engagement quality reviewers are able to complete the review by reviewing selected documentation. We note that Paragraph 11 refers to "engagement documentation...reviewed when performing the procedures required in paragraph 10." We recommend that paragraph 9 also include language to make it clear that the engagement quality review is based upon review of "selected documentation, as considered necessary by the engagement quality reviewer." In addition to being consistent with our understanding of the Board's intent, this change is also consistent with International Standard on Quality Control (ISQC) 1(R) paragraph 37.

Further, we believe that the procedures set forth in paragraphs 10.e. and 10.f. which require the reviewer to "determine if appropriate matters have been communicated, or identified for communication" and "determine if appropriate consultations have taken place on difficult or contentious matters" could be interpreted to require procedures that go beyond the other requirements of the standard that are focused on the evaluation of the work performed by the engagement team. We therefore suggest that the procedures in paragraphs 10.e and 10.f. of the standard be modified as follows to indicate that the engagement quality reviewer should make an evaluation of the appropriateness of such matters based upon performing the other procedures set forth in the standard:

e. ~~Determine if~~ Evaluate whether appropriate matters that are identified through the performance of the other engagement quality review procedures have been communicated, or identified for communication to the audit committee, management, and other parties, such as regulatory bodies.

f. ~~Determine if~~ Evaluate whether appropriate consultations have taken place on difficult or contentious matters that are identified through the performance of the other engagement quality review procedures. Review the documentation, including conclusions, of such consultations.

As an alternative to these revisions, the Board could include these two procedures in a new paragraph which would follow paragraph 10 and clarify that these evaluations should be made based upon the results of all other procedures performed.

We also suggest that the Board modify paragraphs 10.a., 10.b. and 10.d. to make clear that these procedures are intended to apply to significant judgments made by the engagement team. This change is consistent with the direction provided in paragraph 9 and will add appropriate clarity to the requirements. Additionally, to clarify the intended extent of review of planning and the risk assessment process, we suggest that the Board edit paragraphs 10.a. and 10.b. as follows:



a. Evaluate significant conclusions made during engagement planning, including those resulting from the engagement team's –

- ~~The~~ consideration of the firm's recent engagement experience with the company and risks identified in connection with the firm's client acceptance and retention process,
- ~~The~~ consideration of the company's business, recent significant activities, and related financial reporting issues and risks, and
- ~~The~~ significant judgments made about materiality and the effect of those judgments on the engagement strategy.

b. Evaluate the engagement team's identification risk assessments and audit responses, including the identification of significant risks, including fraud risks, and the engagement procedures performed in response to significant risks.

Engagement Quality Review of a Review of Interim Financial Information

As proposed, in a review of interim financial information, the engagement quality reviewer must read the engagement report only if it is filed with the SEC. The final standard should require the engagement quality reviewer to read such a report if one is issued.

Documentation of an Engagement Quality Review

Paragraph 19.c. requires that the engagement documentation include the significant discussions held by the engagement quality reviewer and others who assisted the reviewer, including the date of each discussion, the specific matters discussed, the substance of the discussion, and the participants. We believe the requirement is burdensome and unnecessary, and will result in additional costs that are not likely to provide a commensurate benefit to audit quality. As a result, we recommend it be deleted. For example, an engagement quality reviewer frequently has discussions with the engagement team during the course of an engagement. At the time of each discussion, the engagement quality reviewer may believe it is necessary to document such discussions to ultimately demonstrate compliance with the engagement quality review standard when in fact many of those discussions in retrospect may not be considered to be significant discussions.

The engagement team's existing obligation to prepare documentation consistent with the objective and requirements of PCAOB Auditing Standard No. 3 *Audit Documentation* (AS No. 3), when combined with the proposal's requirement to indicate which documents were reviewed by the engagement quality reviewer and his or her assistants, should provide adequate documentation of the basis for the engagement quality reviewer's compliance with the standard.

Furthermore, we observe that the engagement partner has ultimate responsibility for ensuring that engagement documentation supports the significant judgments made and conclusions reached in accordance with AS No. 3. We do not believe that a requirement in the engagement quality review standard to separately document or supplement documentation of the engagement team's basis for significant judgments made and conclusions reached is necessary or appropriate.

If the Board continues to believe that it is necessary to document oral discussions involving the engagement quality reviewer, we recommend that paragraph 19 be revised to include an explanation of what constitutes a "significant discussion."



Competence of Engagement Quality Reviewer

We agree with the Board that the engagement quality reviewer competency requirement should be “principles-based” and that a general competence standard setting a minimum requirement for the engagement quality reviewer is appropriate. However, we do not believe the language in paragraph 5 of the proposed standard achieves the Board’s intent to establish “a principles-based” requirement. Paragraph 5 does not make it clear that the reviewer’s competence is not required to match that of the engagement partner, and we are concerned that paragraph 5 may have the unintended consequence of prohibiting qualified persons from performing engagement quality reviews. Many judgments are made in the assignment of an engagement quality reviewer including, but not limited to, consideration of the qualifications, experience, and knowledge of both the engagement partner and the potential engagement quality reviewer. As currently worded, paragraph 5 seems to limit the ability to apply such judgment. Furthermore, as indicated in the note to paragraph 6, the engagement quality reviewer is able to obtain assistance from others not associated with the engagement to supplement his or her knowledge. Therefore, we believe that the standard should make clear that the competence requirements contemplate the combined skills of the engagement quality reviewer and any assistants.

In order to provide appropriate flexibility in assigning qualified engagement quality reviewers and provide a principles-based standard that sets a minimum requirement, we suggest paragraph 5 be worded as follows:

The engagement quality reviewer must possess or obtain through utilizing assistants, the level of knowledge and competence related to accounting, auditing, and financial reporting required to serve as the person who has overall responsibility for the same or similar types of engagements. The appropriate level of knowledge and competence depends on the circumstances of the engagement including the size and complexity of the engagement and the engagement quality reviewer's intention and ability to utilize assistants.

Due Professional Care

The proposed standard requires an engagement quality review and concurring approval of issuance for each audit and interim review engagement. The proposed standard indicates that the engagement quality reviewer “may provide concurring approval of issuance only if, after performing with due professional care the review required by this standard, he or she is not aware of a significant engagement deficiency.” We agree with this description of the basis for conclusion, which is consistent with the Board’s interim standard and the overall conclusion of an engagement quality review. The proposal also requires that the engagement quality review be conducted with due professional care. Although we believe the Board’s proposal of a “due professional care” standard of performance is preferable to the “knows or should know” standard of performance previously proposed, we have concern with how “due professional care” has been described by the Board. We respectfully disagree with the Board’s suggestion that “the requirement to exercise due professional care imposes on a reviewer essentially the same requirement as the ‘knows, or should know based on the requirements of this standard’ formulation in the Board’s original proposal.” Additionally, as explained in our comment letter on the original proposal dated May 12, 2008, we remain concerned that “know or should know” imposes additional responsibilities on a reviewing partner beyond those implied by a “due professional care standard.”

Potts v. SEC, 151 F.3d 810 (8th Cir. 1998), which the Board cites, discusses a standard that resembles the “due professional care” standard proposed by the Board (“Having taken on the



concurring review task, Potts also shouldered the duty to perform that task professionally”¹). However, nothing in that decision suggests that due professional care includes engaging in procedures to ensure that there is nothing the reviewing partner “should have known.” Indeed, the SEC’s and the appellate court’s decisions were based on findings that “[Potts] had acted with *reckless disregard* of his duties as an independent auditor”²(emphasis added). His conduct amounted to “an egregious refusal to see the obvious, or to investigate the doubtful.”³ Because its holding was predicated on recklessness, the court had no occasion to consider whether a concurring partner could be liable where he or she “should have known” (but did not “recklessly disregard”) matters that would have caused him or her to withhold concurring approval.

We support the Board’s decision to propose this more preferable *auditing* standard of performance for engagement quality reviewers. The due professional care standard is a standard with which auditors are familiar. It is a clear improvement over the *legalistic* “know or should know” standard previously proposed and avoids the risk of confusing engagement quality reviewers attempting to satisfy it. In light of these considerations, we believe that it is inappropriate for the Board to read into the due professional care standard an element that is not established by precedent and would continue to raise concerns among engagement quality reviewers about the Board’s intent for their performance obligations.

Effective Date of the Proposed Standard

As proposed, the standard would be effective for audits of fiscal years ending on or after December 15, 2009, and for interim reviews in fiscal years beginning after December 15, 2009.

We continue to believe that the proposed effective date would not permit sufficient time for registered public accounting firms to implement the new engagement quality review requirements. Further, we believe that the new standard should be finalized prior the beginning of engagement periods to which it will apply so that the new requirements would (1) be known and anticipated as of the beginning of the engagement period, (2) allow the assigned engagement quality reviewer to comply with the requirements throughout engagement planning and execution, and (3) be in place for each quarterly review conducted under SAS No. 100, *Interim Financial Information*. In this manner, adoption of the new standard would be more effective and efficient.

* * * *

We appreciate the opportunity to provide our perspective to the Board. We would be pleased to discuss our comments and to answer any questions that the PCAOB staff or the Board may have. Please contact Vin Colman (973-236-5390), Jorge Milo (973-236-4300) or Brian Croteau (973-236-4345) regarding our submission.

Sincerely,

A handwritten signature in black ink that reads "Price Waterhouse Coopers LLP". The signature is written in a cursive, flowing style.

¹ See Potts v. SEC, 151 F.3d 810 (8th Cir. 1998). at 813.

² See Id. at 812

³ See Id.



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April 20, 2009

Mr. J. Gordon Seymour
Secretary
Public Company Accounting Oversight Board
1666 K Street, NW
Washington, DC 20006-2803

Re: PCAOB Rulemaking Docket Matter No. 025

Proposed Auditing Standard – Engagement Quality Review

Dear Mr. Seymour,

Reznick Group welcomes this opportunity to respond to the request for comments from the Public Company Accounting Oversight Board (PCAOB) on the proposed auditing standard on *Engagement Quality Review*.

Reznick Group is a national leader in accounting, tax and business advisory services and is ranked among the top 20 public accounting firms in the United States. With offices across the country, Reznick Group serves clients in a broad range of industries that include real estate, emerging businesses, energy, financial services, government, nonprofits, technology and transportation.

This letter offers comments in response to the proposed auditing standard on *Engagement Quality Review* that we believe would be valuable to the PCAOB in making a decision on the final version of the auditing standard.

Comments

We believe that the proposed standard is a significant improvement over the original proposal, and more appropriately reflects the requirements of the engagement quality review. We applaud the Board for the clarifications and amendments made to the proposed standard. However, we believe that a few additional changes would provide further clarification to the final auditing standard. Our comments about these items are provided below.

Paragraph 8 requires that the engagement quality reviewer may not be the person who had overall responsibility for either of the two audits preceding the audit subject to the engagement quality review. This is a change from the SEC independence requirements and is a more restrictive requirement. Currently, the SEC independence requirements allow the concurring partner to be the person who had overall responsibility for the audit



Mr. J. Gordon Seymour
April 20, 2009
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in the immediately preceding year, and could go back and forth every year if needed, but cannot serve more than five years in total before being required to rotate off the client for 5 consecutive years. This change could cause a problem for smaller accounting firms that have fewer resources available to serve clients as either the person with overall responsibility for the engagement or the engagement quality reviewer.

Paragraphs 12 and 17 of the proposed standard states that the engagement quality reviewer may provide concurring approval of issuance only if, after performing with due professional care the review required by the standard, he or she is not aware of a significant engagement deficiency. We applaud the PCAOB for requiring that the engagement quality review be conducted with due professional care, which we believe is preferable to the "knows or should know" standard provided in the original proposal. We believe this change conveys the appropriate degree of performance and is consistent with the objectives and requirements of the proposed standard.

We agree with the PCAOB's observation that due professional care is a concept familiar to auditors and consistent with other auditing standards; however, we respectfully disagree with the PCAOB's statement on page 24 of the release that the requirement to exercise due professional care imposes on a reviewer essentially the same requirement as "knows or should know," which was the condition stated in the PCAOB's original proposal. We believe the condition "knows or should know" imposes significant additional obligations on the engagement quality reviewer and therefore would elicit a level of effort that is not consistent with the objectives and requirements of the proposed standard. As a result, we believe this language should be removed from the release that accompanies the final *Engagement Quality Review* standard.

Paragraph 19(c) states that documentation of an engagement quality review should contain sufficient information to identify the significant discussions held by the engagement quality reviewer and others who assisted the reviewer, including the date of each discussion, the specific matters discussed, the substance of the discussion, and the participants. The engagement quality reviewer may not always know at the time of the discussion whether a given discussion will be significant to the engagement. This requirement would cause the engagement quality reviewer to document every discussion, which would be costly and unnecessary and we believe was not the PCAOB's intent when drafting the proposed standard. Therefore, we believe this requirement is overly onerous, and should be removed from the final standard.

We believe that the effective date of the final *Engagement Quality Review* standard should correspond with the beginning of the audit engagement period to allow for the requirements to be applied to interim reviews and audits in the same fiscal year. This allows the engagement quality reviewer to comply with the requirements of the proposed auditing standard during the audit planning process as well as during the reviews of



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interim financial information. Therefore, we believe that the effective date of the final standard should be for audits of fiscal years beginning on or after December 15, 2009 and for reviews of interim financial information within such fiscal years.

Conclusion

Reznick Group appreciates the opportunity to comment on the proposed auditing standard on *Engagement Quality Review*, and the PCAOB's efforts to adopt a comprehensive standard consistent with Section 103 (a) (2) (A) (ii) of the Sarbanes-Oxley Act.

We would be pleased to discuss our comments further. Please contact Kurtis Wolff at (404) 250-4148.

Sincerely,

Reznick Group, P.C.



April 20, 2009

Office of the Secretary
PCAOB
1666 K Street, N.W.
Washington, DC 20006-2803

RE: PCAOB Rulemaking Docket Matter No. 025
Engagement Quality Review

To Whom It May Concern:

One of the expressed goals of the Texas Society of Certified Public Accountants (TSCPA) is to speak on behalf of its members when such action is in the best interest of its members and serves the cause of Certified Public Accountants in Texas, as well as the public interest. The TSCPA has established a Professional Standards Committee (PSC) to represent those interests on accounting and auditing issues. The PSC has been authorized by the TSCPA Board of Directors to submit comments on matters of interest to the committee membership. The views expressed in this letter have not been approved by the TSCPA Board of Directors or Executive Board and, therefore, should not be construed as representing the views or policy of the TSCPA.

We are delighted to have the opportunity to provide the input of the PSC into your deliberations regarding the repropoed auditing standard, *Engagement Quality Review (EQR)*. Our response includes our answers to the 11 questions listed in the exposure draft.

Question 1: Should the standard require an EQR for other kinds of engagements performed according to PCAOB standards? If so, what types of engagements should be included and what should an EQR of such engagements entail?

We believe the breadth of the standard is sufficient as currently drafted.

Question 2: Is the objective in the repropoed standard appropriately formulated? Does it articulate the purpose of an EQR?

In the letter we submitted on the original draft of this proposed standard, we indicated our support for the inclusion of an objective. We further stated that having an objective was consistent with the move towards the development of principles-based standards. We continue to favor the following objective: "An engagement quality review should be designed to determine: (1) if related financial statements are fairly presented in accordance with generally accepted accounting principles, (2) the internal control is adequate to produce materially reliable financial statements, and (3) the evidence gathered during the audit engagement provided adequate support for the audit opinion."

Question 3: Will this objective contribute to a more thoughtful and effective EQR?

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The objective included in the repropoed standard is vague. The inclusion of an objective in the standard is a positive addition, but we continue to support our suggested objective articulated in the answer to question 2.

Question 4: Is it appropriate to explicitly require a reviewer from within the firm to be a partner or an individual in an equivalent position?

We believe the standard should use wording such as "of sufficient senior status" when describing the status of the reviewer from within the firm. This allows the firm to exercise appropriate judgment and does not tie the decision to a particular title such as "partner."

Question 5: Should the standard allow qualified accountants who are not employed by an accounting firm to conduct the review?

We believe that the standard should allow qualified accountants who are not employed by an accounting firm to conduct the review. It is imperative that the qualifications of the reviewer be specified in the standard. The outside reviewer should have relevant hands-on experience in auditing and financial reporting of SEC registrants, that experience should be current, and the reviewer must be associated with a registered firm. Also, the operating environment of any outside reviewer should be subject to the same oversight by the Board as the firm performing the engagement.

Question 6: Should the standard prohibit the engagement partner from serving as the reviewer for a period of time following his or her last year as the engagement partner? If so, is two years sufficient, or should it be extended?

We find two years to be an acceptable time period.

Question 7: Are the descriptions of the scope and extent of EQR procedures contained in the repropoed standard appropriate? Will the performance of these procedures result in a high-quality EQR? If not, how should these procedures be revised?

Overall, we believe the procedures are appropriate and, if performed completely and with due care and competence, should result in a high-quality EQR.

Question 8: Are the specifically required procedures appropriately tailored to reflect the difference in scope between an audit and an interim review?

We believe the procedures appropriately differentiate between an audit and an interim review.

Question 9: Do the specifically required procedures sufficiently focus the reviewer on areas of highest risk? Are there procedures that should be required?

The specifically required procedures are well designed to direct the reviewer's focus to the areas of high risk. We don't believe the standard should require additional procedures. We feel the quality

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reviewer should use his/her discretion in deciding which, if any, additional procedures need to be performed.

Question 10: Is the standard for the engagement quality reviewer's concurring approval of issuance appropriately described in the reposed standard? Is the first condition appropriately tailored to reflect the difference in scope between an audit and an interim review?

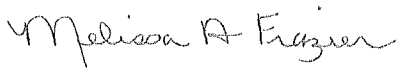
Our response to both issues raised in this question is yes.

Question 11: Are the documentation requirements in the reposed standard appropriate? If not, how should they be changed?

We believe the documentation requirements found in the reposed standard are appropriately focused.

We appreciate the opportunity to provide our input into the standard-setting process.

Sincerely,

A handwritten signature in cursive script that reads "Melissa A. Frazier".

Melissa A. Frazier, CPA
Chair, Professional Standards Committee
Texas Society of Certified Public Accountants



20 April 2009

Our ref: ICAEW Rep 44/09

Office of the Secretary
PCAOB
1666 K Street,
N.W.
Washington
D. C. 20006-2803.

By email: *PCAOB Rulemaking Docket No. 025*

Dear Sir

PCAOB RELEASE NO 2009 - 001: RE-EXPOSURE OF PROPOSED AUDITING STANDARD – ENGAGEMENT QUALITY REVIEW:

The Institute of Chartered Accountants in England and Wales (the 'Institute') welcomes the opportunity to comment on the PCAOB's re-exposure of the proposed auditing standard *Engagement Quality Review*

The Institute operates under a Royal Charter, working in the public interest. Its regulation of its members, in particular its responsibilities in respect of auditors, is overseen by the Financial Reporting Council. As a world leading professional accountancy body, the Institute provides leadership and practical support to over 132,000 members in more than 140 countries, working with governments, regulators and industry in order to ensure the highest standards are maintained. The Institute is a founding member of the Global Accounting Alliance with over 700,000 members worldwide.

Our comments have been prepared with the help of our many members working around the world who have detailed knowledge and practical experience of US, EU and other regulatory regimes.

We applaud the decision of the PCAOB to propose amendments to and re-expose this standard in the light of comments received; it demonstrates a strong commitment to the public interest and a level of responsiveness that will enhance both acceptance of the final standard and the reputation, credibility and standing of the PCAOB itself.

The proposed amendments represent a significant improvement to the original proposals and we are particularly relieved to see the removal of the 'knows, or should have known' formulation together with a replacement based on the auditor's duty to exercise due professional care.

Our outstanding concerns are set out below and we believe that if they are properly addressed, the standard will provide a sound foundation upon which auditors can develop their engagement quality review policies and procedures.



THE INSTITUTE
OF CHARTERED
ACCOUNTANTS

IN ENGLAND AND WALES

We remain concerned that a number of administrative issues, including the proposed applicability of the requirements which we referred to in point 4 of our response to the original exposure, do not appear to have been addressed at all. These issues have not gone away and represent genuine problems for auditors. Guidance from the PCAOB in these areas will help prevent confusion, inconsistencies in approach and problems further down the line. We re-iterate these issues below. **Furthermore, the effective date remains problematic. It seems wholly impracticable for this standard to be mandated for 2009 audits that have already started.**

I would be happy to discuss any of the points raised in this response.

Yours faithfully

Katharine E Bagshaw FCA
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Questions and Answers

1. Should the standard require an EQR for other kinds of engagements performed according to PCAOB standards? If so, what types of engagements should be included and what should an EQR of such engagements entail?

No. The scope is appropriate in the absence of a full framework for audit and assurance engagements in which the PCAOB would need to consider and cover a wide range of engagements to which an EQR might be applicable.

2. Is the objective in the repropoed standard appropriately formulated? Does it articulate the purpose of an EQR?

No. While we are aware that we are in a minority of commentators, we remain of the view that the standard should not state an objective, because it has not been formulated within a framework in which the role and status of objectives are clear. While auditing standards are generally improved by the inclusion of a clear objective, the development of objectives on an *ad hoc* basis is not appropriate. We noted in our response to the original exposure that if an objective is considered necessary, the PCAOB should consider explicitly aligning it with ISAs: ISA 220 requires the engagement quality reviewer to perform an *objective* evaluation.

3. Will this objective contribute to a more thoughtful and effective EQR?

Yes. We concede that the shift of focus from the *process* of the EQR, to the *outcome* that should be achieved is an improvement. The objective refers to significant judgements made by the team rather than (by implication) detailed discussions and procedures.

4. Is it appropriate to explicitly require a reviewer from within the firm to be a partner or an individual in an equivalent position?

Yes. It should be made clear that equivalence is a matter of substance and refers to the sufficiency of appropriate experience and authority in the individual concerned, as required by ISA 220, rather than mere technical equivalence.

The role of persons performing filing reviews, as we note below under *Administrative Matters*, overlap with those of EQRs. Filing reviews under Appendix K of the AICPA SECPS Reference Manual may be performed by individuals who are not partners.

5. Should the standard allow qualified accountants who are not employed by an accounting firm to conduct the review?

Yes. However, paragraph 3 of the proposed standard requires that only associated persons of registered public accounting firms are eligible for appointment as engagement quality reviewers. This appears to conflict with the suggestion on page 12 of the release that reviewers may be retired partners, professors of auditing, or other qualified accountants. It would be helpful if this apparent inconsistency were removed or clarified.

6. Should the standard prohibit the engagement partner from serving as the reviewer for a period of time following his or her last year as the engagement partner? If so, is two years sufficient, or should it be extended?

Yes. We have no objections to this proposal.

7. Are the descriptions of the scope and extent of EQR procedures contained in the repropoed standard appropriate? Will the performance of these procedures result in a high-quality EQR? If not, how should these procedures be revised?

9. Do the specifically required procedures sufficiently focus the reviewer on areas of highest risk? Are there other procedures that should be required?

Yes. The proposed changes to paragraph 10 no longer require the engagement quality reviewer to 'understand' various matters but instead to 'evaluate' work performed by the engagement team in the relevant area. This is an improvement, however,

- there should be more emphasis on the significant judgements brought to the engagement quality reviewer's attention by the engagement partner or team, which would draw attention to matters that might not have been envisaged in the planning, and would align the standard more closely with ISAs
- the 'read', 'review', and 'evaluate' requirements in paragraph 10 are not dealt with by PCAOB Rule 3101: *Certain Terms Used in Auditing and Related Professional Practice Standards*. The PCAOB should consider the need to at least describe the meaning of these terms. 'Review' and 'evaluate' are particularly close terms and 'read' in 10 (g) in particular means little out of context and gives no indication as to the depth of reading required. 'Determine' can be read as requiring or permitting a disproportionately wide range of activities and enquiries.

8. Are the specifically required procedures appropriately tailored to reflect the difference in scope between an audit and an interim review?

Yes.

10. Is the standard for the engagement quality reviewer's concurring approval of issuance appropriately described in the repropoed standard? Is the first condition appropriately tailored to reflect the difference in scope between an audit and an interim review?

Yes.

11. Are the documentation requirements in the repropoed standard appropriate? If not, how should they be changed?

No. Paragraph 19 (c) requires detailed documentation of significant discussions. Avoidance of excessive documentation would be aided by a note to the effect that the 'specific matters discussed' and the 'substance of the discussion' do not require a verbatim record of discussions. Furthermore, in many cases we would expect the

implementation of this standard to result in the audit team documenting more, rather than the engagement quality reviewer filling in the gaps or providing a roadmap as to how the final documentation has evolved.

We also note that the term 'significant' is used liberally in PCAOB standards and is a broad term. Matters of significance, including significant risks, can be straightforward. The focus should be more on significant judgements which may well be more important. The page 17 discussion on 'significant matters' explains significant judgements and this might be brought into the body of the standard.

Administrative Matters

Our response to the original proposals raised concerns and requested clarification on the overlap of the role of the engagement quality reviewer and the filing reviewer under Appendix K of the AICPA SECPS Reference Manual, on component audits, and on the role of inter-office and inter-network/alliance firms. These issues which we summarise below remain unresolved.

- *Overlap of the EQR and the filing review under Appendix K of the AICPA SECPS Reference Manual,*

PCAOB rules currently require certain review procedures to be performed at networked audit firms which are not members of the AICPA. These reviews focus on the application of US accounting audit, disclosure and independence requirements where they are not the usual framework for the reporting firm. The EQR and this review overlap and the PCAOB should give some guidance on how these two requirements can fit together without unnecessary duplication. See also our answer to question 5, above.

- *Referred reporting engagements*

Referred reporting engagements often involve the component auditor confirming that work has been conducted in accordance with PCAOB standards. The proposed standard would require EQRs for component audits. However, in many cases, such judgements are best provided by instructing offices rather than by involving new partners in the reporting office at component level. We recommend that the proposed standard should not apply to component audits.



CENTER FOR CAPITAL MARKETS

C O M P E T I T I V E N E S S

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April 20, 2009

Office of the Secretary
Public Company Accounting Oversight Board
1666 K Street, N.W.
Washington, D.C. 20006-2803

**Re: Public Company Accounting Oversight Board Rulemaking Docket
Matter No. 025**

Dear Members and Staff of the Public Company Accounting Oversight Board:

The United States Chamber of Commerce (“Chamber”) is the world’s largest business federation representing more than 3 million businesses and organizations of every size, sector, and region. The Chamber created the Center for Capital Markets Competitiveness (“CCMC”) to promote a modern and effective regulatory structure for capital markets to fully function in a 21st century economy.

To achieve this objective, it is an important priority of the CCMC to promote an effective financial reporting policy. The CCMC recognizes the vital role of external audits in our markets and supports efforts to maintain and improve audit effectiveness, including by improving quality control and auditing standards. The concurring partner review (engagement quality review (“EQR”)) is a longstanding component of audit firms’ quality control systems and procedures, and so we appreciate the opportunity to comment on the Public Company Accounting Oversight Board (“the Board”) *Proposed Auditing Standard on Engagement Quality Review*. Our comments focus on several important issues raised by the Board’s standard-setting process in general, the approach used in developing the standard under consideration, and specific concerns related to the proposed standard.

Accordingly, the CCMC recommends that the above reference proposed standard be withdrawn and that significant reforms be undertaken to improve the Boards development and implementation of auditing standards.

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Audit Standard Setting Process

The current draft is the second time that the Board has exposed an EQR standard for public comment. The Board's initial draft was proposed on February 28, 2008 ("2008 proposal"), and represented the Board's first new auditing standard, not involving documentation or Section 404 of the Sarbanes-Oxley Act of 2002 ("SOX"). The Board received 38 comment letters on the 2008 proposal – many expressed concerns and confusion over the proposed guidance and the Board's intent as to the role of the EQR. The feedback led to substantive revisions and the need to re-expose the proposed guidance for public comment. However, the nature of the feedback highlights the need of the Board to reconsider its standard-setting approach.

The current standard-setting process lacks both transparency and a sufficient set of stakeholders that have the requisite expertise. As a result, the current process creates uncertainty and undermines clarity and meaning in any proposed standard. These factors complicate the consideration of a proposed standard during the comment process, as occurred with the 2008 proposal, and these complications would be compounded in the implementation of any final standard.

Unlike the Financial Accounting Standards Board ("FASB"), the International Accounting Standards Board ("IASB"), the International Auditing and Assurance Board ("IAASB"), and the Auditing Standards Board ("ASB"), the Board has *not* chosen to develop auditing standards through a transparent process. Outsiders can only observe the open meeting at which the Board votes to issue a proposed or final standard. No transparency exists with the Board's deliberative process for crafting standards. The Board's due process for auditing standards occurs through a formal comment period on a proposed standard. Such formal comment processes are likewise used by the other standard-setting bodies, although their comment processes have been informed by outsiders being able to observe and comment on the deliberations of the standard-setting body along the way.

Furthermore, because the Board appears to rely on an insular procedure without using task forces or other mechanisms to foster outreach, the Board process for developing and drafting auditing standards excludes meaningful contribution from outsiders with current, relevant expertise. Therefore, the Board, in developing new

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standards, does not seek input from the most knowledgeable experts on any particular issue. Therefore, the Board, in developing new standards, does not seek input from a wide range of participants, or the most knowledgeable experts on any particular issue.

The Board has formed a Standing Advisory Group (“SAG”), which is tasked as its external source of advice on standards, including the current proposed EQR standard. SAG consists of thirty or so members, as representatives of various stakeholders in public company audits. While the SAG membership is made up of highly competent individuals, only a few – currently, less than a quarter – are associated with audit firms. Moreover, SAG meetings are limited in frequency and duration. The Board convenes SAG about twice a year for one-day public meetings. While SAG agendas have touched on a variety of issues, the discussions tend to be quite wide-ranging and general, without the focus needed to develop any consensus. Given these factors, SAG has little impact in the development and crafting of auditing standards.

Moreover, SAG meetings do not provide a meaningful forum for open dialogue and interaction with the Board and staff. During SAG meetings, the attending Board members and staff maintain a “listening mode,” based on Board instructions *not* to express views or comments. So, the SAG meetings provide little, if any, insight on the Board or staff thinking on a standard or its development. To illustrate, at the April 2, 2009 SAG meeting, during a discussion of the recently proposed EQR standard, SAG members requested clarification of the Board’s intent in revising the standard to reflect a “due professional care” requirement (par. 12), while the Board stated in the release text that “due professional care” equates to “the same requirement as the knows, or should know” (p. 24). The SAG request was met with silence – no Board or staff member in attendance would respond to this straightforward request.

To address these important issues, we encourage the Board to reconsider its entire approach to standard-setting. The Board is not composed of audit experts and it is unrealistic to expect it to hire a staff of permanent employees that can have or maintain the requisite expertise to formulate standards for *all aspects* of public company audits. Formulating standards requires a breadth and depth of current, relevant audit knowledge and experience. Outside expertise is vital, but the current SAG apparatus does not provide it. Task forces seem to be one of several ways to

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contribute the necessary expertise and contribution of diverse viewpoints to the standard-setting process. Furthermore, we encourage the Board to develop a more transparent and open standard-setting process. For example, dedicated sessions for discussing issues, including sessions for staff education of the Board, could be public. In this way, the views and deliberations of the Board could be better understood by all market participants.

More importantly, SOX Section 103 gives the Board great flexibility in its approach to standard-setting. For example, rather than formulate its own standards, SOX allows the Board to adopt standards proposed by other professional groups of accountants (with or without modification). One logical group that could be tapped into would be the IAASB. And, it is noteworthy that the IAASB has an updated EQR standard.

Adopting standards proposed by the IAASB is likewise consistent with the spirit of convergence. As we have previously expressed,¹ we encourage the Board to embrace the convergence of auditing standards. In continuing to propose its own standards for audits of public companies in the United States, the Board once again fails to acknowledge the globalization of the economy and the unique needs these changes have imposed upon businesses and investors alike. Commonalities in the dissemination, reliability, and evaluation of financial information assist in the sound operation of markets. With this proposal, as currently constituted, the Board has missed an opportunity to advance the convergence of international auditing standards.

EQR Objective and the Standard of Care for Performing an EQR

As noted, the 2008 proposal generated a good deal of consternation and concern. The Board has revised the wording of the current proposed standard in an attempt to address the issues raised by previous commenter's. Nonetheless, in several important areas, the Board appears to temper its revisions within the standard and through the use of release text, actually modifies the standard and undermining its intent and meaning. Essentially, the Board appears to be maintaining its prior

¹ For example, see letter from the United States Chamber of Commerce's Center for Capital Markets Competitiveness on PCAOB rulemaking docket matter No. 026, *Proposed Auditing Standards Related to the Auditor's Assessment of and Response to Risk* (February 18, 2009).

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positions as put forth in the 2008 proposal, in spite of the revisions set forth in the proposed standard under consideration. These inconsistencies will certainly create confusion in the implementation and enforcement of such a standard. For example, release text is often used to interpret the Board's standards as part of inspection, private litigation, and regulatory enforcement activities. Two important areas in which inconsistencies occur between the proposed standard and release text involve the objective of the EQR and the standard of care for performing an EQR.

A. *EQR Objective*

The proposed standard states that the objective of the EQR "is to perform an evaluation of the significant judgments made by the engagement team and the conclusions reached in forming the overall conclusion on the engagement and in preparing the engagement report, if a report is to be issued, in order to determine whether to provide concurring approval of issuance" (par. 2). This seems a reasonable objective.

On the other hand, subsequent paragraphs in the proposed standard modify this objective by stating, for example, that: "[i]n an audit, the engagement reviewer may provide concurring approval of issuance only if, after performing with due professional care the review required by this standard, he or she is not aware of a significant engagement deficiency" (par. 12). This is followed by a note that explains a "significant engagement deficiency in an audit exists when (1) the engagement team failed to obtain sufficient appropriate evidence in accordance with the standards of the Board, (2) the engagement team reached an inappropriate overall conclusion on the subject matter of the engagement, (3) the engagement report is not appropriate in the circumstances, or (4) the firm is not independent of its client" (par. 12). Furthermore, based on paragraph 12 (for an audit), due professional care applies to the EQR required by the standard as a whole, and is not limited to the conduct of the EQR requirements in paragraphs 9, 10, and 11. Thus, the language in paragraph 12 (including the note) appears to considerably broaden the original objective of the EQR, as stated in paragraph 2, from evaluating significant judgments by the engagement team to searching for possible engagement deficiencies.

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To help address this issue for audits, we recommend that the Board revise paragraph 12, confine the conduct of the EQR to the requirements in paragraphs 9, 10, and 11, and eliminate the note (and make a similar revision to paragraph 17 for interim reviews, to confine the conduct of the EQR to the requirements in paragraphs 14, 15, and 16). For example, we suggest the following wording for paragraph 12: “In an audit, the engagement reviewer may provide concurring approval of issuance only if, after performing with due professional care the requirements in paragraphs 9, 10, and 11, he or she is not aware of any matters that would cause him or her to believe that the financial statements are not in conformity with generally accepted accounting principles in all material respects, or that the firm’s audit was not performed in accordance with the Board’s auditing standards.”

This suggested clarification is of added importance because the release text in several places does not reiterate paragraph 2, rather the release text states that the objective of the EQR is to detect any significant engagement deficiencies. For example, the release text says that the “[e]ngagement quality review (‘EQR’) is an opportunity for the auditor to discover any significant engagement deficiencies” (p. 2). Also, the release text says “...the Board continues to believe that in order to improve audit quality, the standard must require an EQR that serves as a meaningful way to identify significant engagement deficiencies in time to correct them” (p. 4).

It is noteworthy that identifying significant engagement deficiencies is an objective of the Board’s inspection. So, the question naturally arises, in spite of the stated objective in the proposed standard (par. 2), whether the Board continues to equate the EQR review with an inspection, albeit with the distinction that the EQR is performed prior to the release of the auditor’s report. Such a view would be consistent with the position expressed by one Board member at the 2008 open meeting, who said that “...a thoughtful engagement quality reviewer – who after all has access to the same information we do as part of our inspections – could have found and focused the firm on these deficiencies before we inspected the firm.”² But, of course, the EQR reviewer does not have the same information as a Board inspector. Not only does the available information change post-issuance of the audit

² Statement of Board Member Charles D. Niemeier at the PCAOB February 26, 2008 Open Meeting on the *Proposed Auditing Standard on Engagement Quality Review*.

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report and with the passage of time, but the inspection process typically involves a team of people that follow different procedures and processes than an EQR reviewer. It is simply inappropriate to conflate Board inspections and EQRs.

B. *Standard of Care for Performing the EQR*

Further compounding the confusion about the Board's intent with respect to the role of the EQR is the inconsistency between the proposed guidance and the release text as to the standard of care for performing an EQR. As previously noted, the proposed standard refers to "due professional care" and references AU Section 230, *Due Professional Care in the Performance of Work*. However, in the release text, the Board undermines the use of "due professional care" and alters its current meaning in the professional literature by stating: "While auditors should be more familiar with 'due professional care' than the concurring approval standard in the original proposal, the requirement to exercise due professional care imposes on a reviewer essentially the same requirement as the 'knows, or should know based on the requirements of this standard' formulation in the Board's original proposal" (p. 24).

A standard of "knows, or should know" is akin to a strict liability requirement for engagement deficiencies. The proposal not only would impose a new legal standard, but does so through the backdoor of release text and contravenes both audit standards and the legislative process. Moreover, it imposes this new standard on all auditors – not just EQR reviewers – because the release text will be used by plaintiff attorneys, Board inspectors, and other regulators as indicative of the Board's definition of due care, in spite of AU Section 230. As such, the "knows, or should know" definition of due care in the release text significantly exacerbates litigation risk and sustainability concerns for public company auditors. In both concept and application, this is simply unacceptable and the entire first paragraph on page 24 of the release text should be deleted.

Other Comments

We have two additional comments on the specifics of the proposed standard related to the qualifications of the EQR reviewer and the effective date of the proposed standard. The proposed standard responds to a good deal of feedback that

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the Board received on these two matters. However issues still remain in the latest proposal.

A. *Qualifications of an Engagement Quality Reviewer*

The *existing* quality control requirements call for partners to conduct EQRs, although the Boards Rule 3400T allows that audit firms may seek a waiver to engage an academic or other experienced accountant to perform the EQR. Setting aside whether academics generally would have the requisite experience and expertise to serve as EQR reviewers, the Board has provided no information on how many audit firms have sought or been granted such waivers. However, given the lessons we are learning from the Madoff fraud, the Board should be cautious about promulgating a standard that retrenches on any existing requirements for EQR reviewers with respect to smaller firms.

The proposed standard has a general competence requirement and otherwise requires independence, integrity, and objectivity. However, it does not appear to sufficiently appreciate that competence comes from experience for all EQR reviewers. And, it does not appreciate the necessity of ensuring requisite authority for reviewers from outside the firm. In regards to these two issues, and consistent with our comments on the need for the Board to embrace the convergence of auditing standards, it would be worthwhile for the Board to consider the requirements of the IAASB in International Standards on Auditing (“ISA”) 220. ISA 220, which has been through due process, explicitly recognizes the need for both experience and authority by defining the engagement quality control reviewer as “a partner, other person in the firm, suitably qualified external person, or a team made up of such individuals, with sufficient and appropriate experience and authority to objectively evaluate, before the auditor’s report is issued, the significant judgments the engagement team made and the conclusions they reached in formulating the auditor’s report.” As such, ISA 220 provides a *higher threshold* for serving as an EQR reviewer than that in the Board’s proposed standard.

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B. *Effective Date of the Proposed Standard*

The Board intends to make a final standard effective, subject to approval by the Securities and Exchange Commission (“SEC”), for fiscal years *beginning* after December 15, 2009 for EQRs of interim reviews. However, for EQRs of audits, the Board intends to make a final standard effective, subject to SEC approval, for audits of fiscal years *ending* on or after December 15, 2009. The Board expressed sympathy for concerns expressed by commenter’s on the 2008 proposal that implementing any new EQR requirements in the middle of an engagement could be disruptive. Nonetheless, the Board concluded that “it is important to strengthen the existing requirements as soon as practicable” (p. 27).

The CCMC respectfully disagrees that the proposed standard is a strengthening of the existing requirements. In addition, it is not practicable to implement a final standard in 2009. Given the time required for the Board to consider comments, prepare, and approve a standard and then for SEC to consider the Board’s standard, including the requisite SEC public comment process and vote by the Commission, implementation in 2009 is not feasible. It should simply be abandoned as a goal.

Responsibility for any delays in promulgating a new EQR standard resides with the Board. The Board should not impose hardships on audit firms and EQR reviewers because of problems with the Board’s standard-setting process.

Conclusion

In conclusion, we appreciate the opportunity to comment on the Board’s *Proposed Auditing Standard on Engagement Quality Review*. It is important to ensure that the Board gets the guidance right. Likewise, it is important to ensure that the Board avoids confusing or undermining any guidance through inconsistent statements; in particular in the release text that accompanies any final standard.

However, given the substantive nature of our comments, the CCMC remains concerned that the proposed standard represents a step backward. Accordingly, it is respectfully submitted that the Board should withdraw the proposed standard and

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extend the current EQR requirements to all registered audit firms,³ while it deliberates its next steps.

Finally and most importantly, it is apparent that the Board's standard setting process needs to be reformed. The CCMC strongly encourages the Board to address this challenge, and stands ready to assist the Board in any manner.

Sincerely,

A handwritten signature in black ink, appearing to read "Richard Murray", with a long, sweeping tail extending downwards and to the right.

Richard Murray
Chairman
U.S. Chamber of Commerce
Center for Capital Markets Competitiveness

³ See Statement of Board Member Bill Gradison at the March 4, 2009 Open Meeting on *Proposed Auditing Standard on Engagement Quality Review*.



United States Government Accountability Office
Washington, DC 20548

April 16, 2009

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. 2009-001,
Proposed Auditing Standard -- *Engagement Quality Review*

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

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. Holding the April 2, 2009, Standing Advisory Group (SAG) meeting during the exposure period and including discussion of the proposed standard was especially helpful in improving the transparency of the standard-setting process and developing a broad consensus on the issues discussed. We encourage the PCAOB to hold a SAG meeting whenever proposing a major standard.

We continue to believe that the public interest would be better served if the PCAOB adopted the standards of the International Auditing and Assurance Standards Board (IAASB), or the AICPA's Auditing Standards Board (ASB), and added incremental standards as necessary and appropriate for audits of U.S. registered companies. The PCAOB's 2009 proposed standard is more consistent with international standards than its previous draft; however, we believe the public would be better served by having the PCAOB adopt International Standard on Auditing (ISA) 220, *Quality Control for an Audit of Financial Systems*, or the corresponding proposed Statement on Auditing Standards (SAS) to eliminate remaining differences which, we believe, are significant. The PCAOB could then supplement the general principles and guidance in the ISA if they consider it necessary and appropriate.

We are concerned that important differences remain between the PCAOB's 2009 proposed standard and the IAASB's audit and quality control standards. The ISA and the related International Standard on Quality Control (ISQC) focus more appropriately on the substance of an engagement quality review and the general principles to be applied, while this PCAOB draft addresses specific requirements and processes for an EQR. This difference in approach is particularly noticeable in the following areas: (a) reviewer qualifications, and (b) documentation.

(a) Reviewer Qualifications (Questions 4, 5, and 6)

The PCAOB's 2009 proposed standard includes a prescriptive, detailed list of reviewer requirements. While the introductory material emphasizes the importance of considering the authority of the reviewer, this essential qualification is not discussed in the standard. Instead, the standard requires a partner (or equivalent) to perform an engagement quality review.

By contrast, ISA 220 is a more principles based standard. The ISA indicates in paragraph 7(c) that an engagement quality control reviewer is "A partner, other person in the firm, suitably qualified external person, or a team made up of such individuals, none of whom is part of the engagement team, with sufficient and appropriate experience and authority to objectively evaluate the significant judgments the engagement team made and the conclusions it reached in formulating the auditor's report." Similarly, ISQC 1, paragraphs A47-51 provide broad guidance for evaluating reviewer expertise, experience, authority, and objectivity.

(b) Documentation (Question 11)

The PCAOB's 2009 proposed standard, specifically paragraph 19 b and c, includes specific documentation requirements that appear to overlap and duplicate the documentation requirements in PCAOB's AS No. 3, Audit Documentation, as the audit team would also document such matters.

Paragraph 19: Documentation of an engagement quality review should be included in the engagement documentation and should contain sufficient information to identify:

- a. The engagement quality reviewer and others who assisted the reviewer,
- b. The documents reviewed by the engagement quality reviewer and others who assisted the reviewer,**
- c. The significant discussions held by the engagement quality reviewer and others who assisted the reviewer, including the date of each discussion, the specific matters discussed, the substance of the discussion, and the participants, and**
- d. The date the engagement quality reviewer provided concurring approval of issuance or, if no concurring approval of issuance was provided, the reasons for not providing the approval. [bolding added for emphasis]

We believe that the EQR documentation requirements in ISA 220 are more appropriate, as they document satisfaction of the objectives of the EQR, rather than the detailed issues discussed and process of the EQR. ISA 220 paragraph 25 states that:

Paragraph 25: The engagement quality control reviewer shall document, for the audit engagement reviewed, that:

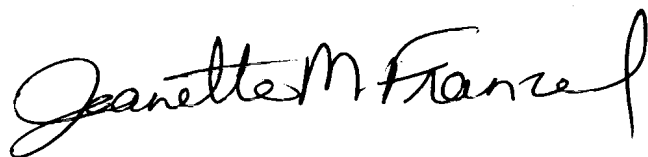
- a. The procedures required by the firm's policies on engagement quality control review have been performed;
- b. The engagement quality control review has been completed on or before the date of the auditor's report; and
- c. The reviewer is not aware of any unresolved matters that would cause the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

Finally, inconsistencies between the PCAOB 2009 proposed standard and the accompanying introductory material may result in confusion and misapplication of the standard. For example, while the standard states in paragraph 3 that a reviewer may be a partner or partner equivalent, indicating that this is a qualification for firms to consider, the introductory material states that "the new standard explicitly requires a reviewer who is employed by the firm issuing the report to be a partner (or a person in an equivalent position)."[underlining added for emphasis] A similar inconsistency exists between the discussion in paragraph 12 of the standard on due professional care, which refers to the generally accepted standard in AU sec. 230, and the guidance on page 24 of the introductory material, which states that "the requirement to exercise due professional care imposes on a reviewer essentially the same requirement as the "knows, or should know based on the requirements of this standard" formulation in the Board's original proposal."

If the Board believes, based on its inspections, that additional requirements or guidance is necessary, the PCAOB should develop clear, incremental standards and explain why they believe such incremental standards are necessary and appropriate for engagement quality reviews of audits of U.S. registered companies.

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

Sincerely yours,



Jeanette M. Franzel
Managing Director
Financial Management and Assurance

Enclosures

cc: The Honorable Mary L. Shapiro, Chairman
Securities and Exchange Commission

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

James L. Kroeker, Acting Chief Accountant
Securities and Exchange Commission

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



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April 17, 2009

Mr. J. Gordon Seymour
Secretary, Public Company Accounting Oversight Board
1666 K Street, NW
Washington, DC. 20006-2803

PCAOB Rule Making Docket Matter No. 025 – Engagement Quality
Reviews

Dear Sirs:

The purpose of this letter is to expand upon the comments I and others made at the Standing Advisory Group (SAG) meeting of April 2, 2009 on the subject of Engagement Quality Reviews (EQR), and in doing so to express the views of Xerox Corporation on this subject. Xerox Corporation is a multinational technology and document services organization with operations in over 130 countries. Our audit fees, exclusive of non-recurring items and non audit services, have approximated \$20 million in recent years. Xerox is a calendar year reporting entity and in recent years we have traditionally been a very early filer of our interim and annual reports on Forms 10-Q and 10-K respectively. For example, our 2008 Form 10-K was filed on February 13, 2009 – 43 days after year end and 17 days earlier than required. Accordingly, any regulatory rule making proposal that potentially affects the aggregate cost of audit services and/or the timing of the completion of interim and annual audit procedures is of interest to us.

Before I provide detailed comments in several areas, let me begin by commending the PCAOB (the "Board), the Chief Auditor and staff for the improvements made to the original EQR proposal issued on February 26, 2008. The current EQR proposal dated March 4, 2009 in general represents a very readable and operational document and clearly demonstrates professional responsiveness to the issues raised during the comment letter process associated with the original EQR proposal.

My specific comments on scope, concurring review and documentation follow and in general build upon discussions at the April SAG meeting.



Scope

With one exception, I concur with limiting the scope of EQRs to regular interim reviews and annual audits. Most other types of audit and audit related engagements either: do not rise to same level of importance as audits or interim reviews; are not by their nature intended to directly benefit or be relied upon current or future shareholders; or due to the time is of the essence nature of certain services (such as a long form M&A due diligence report) it is not normally practical to involve a concurring review partner. The one exception – the one that I raised at the SAG meeting – is for the Board to consider including SAS 70 engagements, in particular SAS 70 Type 2 engagements, on internal controls for service providers, within the scope of the final standard. For many corporations today, large portions of transaction processing and record keeping are outsourced and off-shored. A large multinational company may receive a score or more of SAS 70 Type 2 reports each year. These reports are critical to the receiving company and its auditors particularly with respect to the annual audit of internal controls. If these functions were kept in house the audit procedures necessary to attest to the internal controls and resultant balances would clearly be subject to an EQR. The fact that these functions are no longer under the direct control of a company does not relieve the company (or its auditors) from responsibility in the event that an error therein results in a material error in the consolidated financial statements.

Accordingly, I recommend that if the engagement to be performed is to prepare a SAS 70 Type 2 report that the underlying engagement also be included within the scope of any final EQR standard.

Concurring Approval

My comments in this section relate to the interaction of the phrases 'due professional care' and 'knows or should have known'. The Board is to be commended for addressing the concerns raised by commentators in response to the original EQR proposal by removing the phrase 'knows or should have known' from the revised EQR Exposure Draft. You will recall, however, at the April SAG meeting much discussion centered around the observation that the covering Release to the Exposure Draft left intact the phrase 'knows or should have known' in the explanatory sections of the document. The Release went on to state such phrase essentially imposes the same requirements as the long standing requirement for an auditor to exercise 'due professional care'. The purpose of this comment letter is not to express a view as to whether or not these phrases are synonymous. It appears to this SAG member that the room was extremely divided on the subject in that the Board and staff believed the phrases were essentially equal in meaning whereas most, if not all, of the



accounting firms present believed they meant very different things. I have two specific comments.

- First, the needs of both proponents and opponents can be achieved by using only the phrase 'due professional care' in any document (the final Standard, covering Release, etc.) plus related follow on communications such as staff speeches. If the phrases in fact mean the same thing then there is no need for the redundancy. Conversely if they do in fact mean different things then limiting the final Release and Standard to referencing only 'due professional care' will clearly address the concerns arising from the original EQR proposal.
- Second, as I observed at the meeting it is important to keep in mind that while an official accounting or auditing standard may be the literal requirement(s) it is frequently the collateral materials that are critical – whether it be the 'Basis for Conclusions' or "Background Information' in FASB pronouncements or in the covering PCAOB and SEC Releases for new regulatory requirements – to an understanding of what the authors believe the issues to be, what problems were trying to be solved, how the interpretation of the requirements will likely evolve, etc. Consequently, I can understand why the SAG members from the public accounting firms are concerned about leaving the phrase 'knows or should have known' in the covering Release and I recommend it be removed from the entirety of any final documents on EQR requirements.

Should the Board conclude the final Standard (or covering Release and related documents, etc.) needs to include the phrase 'knows or should have known', I recommend the context be clarified to the effect that: "...knows or should have known is intended by the Board to apply only to *matters brought by the engagement team to the attention of the engagement quality reviewer or in response to inquires of the engagement team by the engagement quality reviewer...*" (emphasis added). I believe phraseology to this effect will address the concern that 'knows or should have known' is not intended to be a second audit.

Documentation

At the SAG meeting there was considerable discussion about the documentation requirements of an EQR with most of it centered on paragraph 19.c of the Exposure Draft. After reflection it does appear that the requirements of paragraph 19.c will frequently be excessive of what is necessary in the normal circumstance. Accordingly I recommend the Board and staff re-visit this section prior to finalizing the EQR requirements – particularly with respect to the requirement to document 'each discussion' – and consider if there is a way the documentation burden can be reduced. Since the purpose of an EQR is to improve an



audit I believe it should be left to the judgment of the engagement team and the engagement quality reviewer to determine the extent to which documentation is needed with respect to the items considered by the reviewer. Obviously some form of EQR documentation is critical. Whether it is in the form of a discrete package of potentially extensive material prepared by the reviewer or, alternatively, it is prepared by the engagement team and distributed throughout the engagement's overall documentation is not critical. The important objective is for a high quality EQR to enhance the overall audit performance and the documentation requirements should be drafted consistent with this objective.

* * * * *

In summary, I believe the current Exposure Draft represents a significant improvement over the original proposal of February 2008 and reflects a serious effort by the Board and staff to address constituent concerns arising from the comment letter process. Before the EQR Standard is finalized, I recommend: (1) the Board deliberate the inclusion of SAS 70 Type 2 engagements within the scope of services subject to the standard; (2) the phrase 'knows or should have known' be removed from any covering Release or related communications distributing the new EQR Standard (which presumably will continue to omit such language as well) and (3) the Board reconsider the documentation requirements of paragraph 19.c which a number of SAG members observed appeared to be excessive in normal situations.

Please do not hesitate to contact me at 203-849-2630 if you have any questions or comments about the contents of this letter.

Yours very truly,

A handwritten signature in cursive script, appearing to read "Gary R. Kabureck".

Gary R. Kabureck

NOTICE: This is an unofficial transcript of the portion of the Public Company Accounting Oversight Board's Standing Advisory Group meeting on April 2, 2009 that related to the Board's proposed auditing standard titled "Engagement Quality Review." The other topics discussed during the April 2, 2009 meeting, including audit confirmations, emerging issues, and going concern, were not related to the proposed auditing standard. Those discussions are not included in the transcript.

The Public Company Accounting Oversight Board does not certify the accuracy of this unofficial transcript. The transcript has not been edited and may contain typographical or other errors or omissions. An archive of the webcast of the entire meeting can be found on the Public Company Accounting Oversight Board's website at http://www.pcaobus.org/News_and_Events/Webcasts.aspx.

1 PUBLIC COMPANY ACCOUNTING OVERSIGHT BOARD (PCAOB)

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3 STANDING ADVISORY GROUP MEETING

4

5

6 8:32 a.m.

7

8 Thursday, April 2, 2009

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11 National Association of Home Builders

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13 1201 15th Street, N.W.

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15 Washington, D.C.

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1 So with that, I'd like to move to the first
2 item on the agenda, engagement quality review, and
3 I'll turn that over to Greg Scates, who will lead that
4 discussion.

5 GREG SCATES: Thank you, Jennifer.

6 As you are aware, soon after the board's
7 creation, the board adopted certain existing standards
8 used by the auditing profession. One such standard
9 was the concurring partner review requirement, which
10 the board continued to apply on a transitional basis
11 to register firms that were members of the SEC
12 Practice Section of the AICPA as of April of 2003.

13 Registered accounting firms that were not
14 members of the SEC Practice Section, those were
15 generally non-U.S. firms and some smaller firms, are
16 not subject to this existing requirement.

17 As part of the board's process of evaluating
18 the existing concurring partner review requirement,
19 the board sought the advice of the Standing Advisory
20 Group on two separate occasions, in June of 2004 and
21 October of 2005. In addition to input received at
22 these SAG meetings, the board considered information
23 on this topic from PCAOB inspections, SEC and PCAOB

1 enforcement cases, and other sources.

2 On February 26 of last year, of 2008, the
3 board proposed to replace the existing requirement
4 with a new auditing standard entitled Engagement
5 Quality Review. The board received 38 comment letters
6 on this proposal and, in response to the comments,
7 made significant changes to the original proposal. On
8 March 4th of this year, the board re-proposed the
9 standard. The comment period for this re-proposal
10 ends on April 20th.

11 A transcript of the discussion this morning
12 will be available on our website, along with the
13 comment letters that we received.

14 Today we'd like to discuss certain aspects
15 of the proposed standard that generated significant
16 feedback from commenters on the original proposal. In
17 particular, the SAG will discuss questions from the
18 release related to reviewer qualifications, the
19 engagement quality review process, concurring approval
20 of issuance, and documentation of the engagement
21 quality review.

22 So first, let's turn to reviewer
23 qualifications. The board originally proposed to

1 allow the engagement quality reviewer to be a partner
2 or another individual in the firm or an individual
3 outside the firm. In contrast, as described in the
4 release on March 4th, the new proposal would require a
5 reviewer from inside the firm to be a partner or a
6 person in an equivalent position. Like the original
7 proposal, the new proposal would allow a qualified
8 person outside the firm to perform this review.

9 In addition, as under the original proposal,
10 the reviewer must have independence, integrity, and
11 objectivity, and must possess the level of knowledge
12 and competence required to serve as the engagement
13 partner for the same type of engagement.

14 The discussion questions on reviewer
15 qualifications taken from the release are on the slide
16 in front of you. These are the ones we'd like to talk
17 about first. Is it appropriate to explicitly require
18 a reviewer from within the firm to be a partner or an
19 individual in an equivalent position? Should the
20 standard allow qualified accountants who are not
21 employed by the accounting firm to conduct the review?
22 And then should the standard prohibit the engagement
23 partner from serving as a reviewer for a period of

1 time following his or her last year as the engagement
2 partner? And if so, is two years a sufficient time,
3 or should it be extended?

4 So I'd like to go ahead and open up our
5 discussion here on the reviewer qualifications for the
6 engagement quality reviewer.

7 JENNIFER RAND: Just for the new members, if
8 you're interested in making comments, we'll try to
9 call on you in order. If you could just please put
10 your name tent on the side, and we'll get to you.

11 GREG SCATES: I'm sorry. Wayne? Wayne
12 Kolins?

13 WAYNE KOLINS: Yes. I'm just thinking on
14 the first one, I think it is appropriate for the
15 reviewer to be a partner, and I would just seek some
16 clarification in terms of what "equivalent position"
17 means. I assume that if the accounting firm is not
18 organized as a partnership, then we're talking about a
19 name other than a partner, but an equivalent to what a
20 partner would be in a partnership.

21 GREG SCATES: Yes. We explain that in the
22 release. Yes, you are correct, Wayne, that if it's
23 structured like a corporation, then they're sometimes

1 referred to as members, and it would be someone in an
2 equivalent position as a partner.

3 WAYNE KOLINS: And I do think it is
4 appropriate for those that are not employed by the
5 firm, and particularly with respect to smaller
6 accounting firms. They may have a resource issue
7 getting the number of partners to serve as a
8 concurring reviewer, and it has been the experience
9 for such firms to go outside the firm, perhaps getting
10 an accounting professor, an audit professor, or
11 somebody that is very experienced doing these reviews,
12 and I think that's an appropriate objective and
13 provision for the standard.

14 GREG SCATES: Thank you, Wayne.

15 Hal Schroeder?

16 HAROLD SCHROEDER: I was curious about the
17 second requirement or applicability of hiring somebody
18 from the outside. How do you handle the independence
19 issue? It seems like if you find someone, as was just
20 suggested, a professor or someone who develops I would
21 say a specialty in being this reviewer, will they
22 become dependent on that stream, and would they tend
23 to shade their views to make sure they had that steady

1 stream of being the reviewer? They may be qualified,
2 but their source of income may make them less than
3 independent.

4 GREG SCATES: Good point. Thank you, Hal.

5 Gaylen Hansen?

6 GAYLEN HANSEN: I would follow up with
7 Wayne's comments. I agree that perhaps some
8 clarification on what equivalent position within the
9 firm means, what may be a little bit of color on that,
10 if it were.

11 But at the same time, on the other question
12 about the outside reviewer, I think the same standard
13 should apply. I don't know how you have a lesser
14 standard with outside individuals than what you would
15 within the firm, and the follow-up with the last
16 comment. I think the independence issue is typically
17 resolved with respect to either that individual is
18 with another registered firm and some sort of
19 independence confirmation that there's independence,
20 in fact, with that client.

21 On the third question about the prohibition
22 of becoming an engagement quality reviewer after
23 serving as an engagement partner if you still have

1 years open within the five-year rotation period, I
2 think some break is appropriate. I'm not sure where
3 the two years came from or why it was thought that
4 that would be appropriate. I would even ask, in the
5 interest of smaller firms that have limited resources,
6 whether a one-year break would be sufficient. I'm not
7 sure that two years is necessary.

8 GREG SCATES: Bernard Jarvis?

9 BERNARD JARVIS: It's my view also that the
10 engagement quality review is a very important part of
11 the audit and ought to be assigned to a person who is
12 a senior executive in the firm, and that would, in my
13 opinion, be someone at the partner level. And I'd
14 just address the third point. I agree with Gaylen
15 that perhaps in the case of small firms, one year
16 break. I do agree that some break is necessary, and
17 I'd agree that about one year would be sufficient.

18 GREG SCATES: Other comments on the
19 qualifications? Joe Carcello?

20 JOSEPH CARCELLO: I appreciate the sentiment
21 on the one year. The one thing you probably need to
22 think about carefully, though, since your purview is
23 public companies, is two years of balance sheets and

1 three years of income statements and cash flow
2 statements in the 10-K. And so if there's a one-year
3 period after someone rolls off being the engagement
4 partner and they come on and they're the engagement
5 quality reviewer, at least some of the financial
6 information and the financial statements that they're
7 going to be reviewing were financial statements that
8 they were responsible for auditing.

9 GREG SCATES: Any other comments on the
10 reviewer qualifications? Arnold Schilder?

11 ARNOLD SCHILDER: Thank you. Just a brief
12 comment for agreement with what you have done. If I
13 compare it with what the IAAHB has done in the quality
14 control standard, you've tried also to define a bit of
15 a general principle which mentions more general
16 principles, sufficient and appropriate technical
17 expertise, experience, and authority, because you can
18 never, let's say, regulate all detailed circumstances.
19 So we thought it was helpful to have a bit of a
20 broader criteria to which against you can judge the
21 more specific criteria. And I would just offer that
22 as a thought that might be helpful in the
23 circumstances.

1 GREG SCATES: Thank you, Arnold.

2 If there are no other comments, we can move
3 to the next topic. Let's turn to the engagement
4 quality review process.

5 It's described in the release under the new
6 proposal like the original proposal. It would require
7 evaluation of significant judgments made and
8 conclusions reached by the engagement team, and
9 specify certain procedures that the reviewer should
10 always perform. The new proposal provides that the
11 reviewer should perform these procedures through
12 discussions with the engagement team and through the
13 review of documents.

14 Under the original proposal, after
15 performing certain procedures, the reviewer was
16 required to perform additional procedures in higher
17 risk areas of the engagement. This provision is not
18 included in the new proposal because the board
19 believes that the required procedures are sufficient
20 to focus the reviewer on the areas of higher risk.

21 The new proposal describes specific
22 requirements for an engagement quality review of an
23 interim review. These requirements are based on the

1 proposed requirements for an engagement quality review
2 of an audit and are tailored to the different
3 procedures performed in a review of interim financial
4 information.

5 Now let's turn to the questions in the
6 release on the engagement quality review process, as
7 on the screen in front of you. Are the descriptions
8 of the scope and extent of engagement quality review
9 procedures contained in the re-proposed standard
10 appropriate? Will the performance of these procedures
11 result in a high-quality engagement quality review?
12 If not, how should these procedures be revised? Are
13 these specifically required procedures appropriately
14 tailored to reflect the difference in scope between an
15 audit and an interim review? And then lastly, do the
16 specifically required procedures sufficiently focus
17 the reviewer on areas of higher risk? Are there other
18 procedures that should be required?

19 I'm going to open up the floor for
20 discussion of the engagement quality review process
21 itself.

22 Wayne Kolins?

23 WAYNE KOLINS: One process, part of the

1 process that I'd like to see put in there is some
2 guidance or some principle regarding how any
3 differences of opinion between the engagement quality
4 reviewer and the engagement partner are worked out.

5 GREG SCATES: Okay. Gaylen Hansen?

6 GAYLEN HANSEN: Yes, I think that resolution
7 process needs to be addressed that Wayne just brought
8 up.

9 The other thing that I think would be
10 helpful is some sort of distinction between
11 materiality with respect to an audit and a 10-Q
12 interim review would seem to be appropriate in the
13 sense that materiality in an audit -- and we all
14 struggled with that, and we've had those discussions
15 around this table, but it involves planning and
16 understanding of the system and internal controls,
17 whereas I think there's a little bit different meaning
18 of materiality on interim reviews, and there doesn't
19 seem to be any kind of distinction with respect to
20 that and how that is addressed. It talks about
21 material modifications and the AU -- what is it? 722?
22 -- and I think if a little bit more was said about
23 that particular distinction, it would be helpful.

1 GREG SCATES: Randy Fletchall?

2 RANDY FLETCHALL: Greg, I would just like to
3 comment, first to commend the board. I think the
4 revisions that were made from the first version to
5 this version went a long way in clarifying what I
6 think were some concerns about what exactly is the
7 process that the standard is articulating.

8 I think likewise the original version, an
9 audit and interim review were kind of lumped together,
10 and so now I think it's much clearer that those are
11 different service levels and the level of the
12 engagement review is different.

13 Undoubtedly, we will still have a few
14 comments on a few words that we would suggest,
15 probably Paragraphs 9 and 10, maybe an addition to
16 that section that would give some additional
17 clarification. But I guess I would just say I think
18 this went a long way in solving what we thought were
19 some of the concerns.

20 GREG SCATES: Thank you, Randy.

21 Greg Jonas?

22 GREGORY JONAS: I am a little surprised that
23 the document doesn't give more attention to the issue

1 of timing of the review. In my experience, a key
2 differentiating factor between substantive concurring
3 partner reviews and non-substantive, often the root
4 cause was the concurring partner was in late,
5 particularly on larger engagements where audits are
6 kind of like aircraft carriers. If you don't turn
7 them on a dime, you don't turn them quickly. You've
8 got to get a running start.

9 The concurring partner, looking at planning
10 shortly after the planning is done, looking at the
11 resolution of major issues as they occur throughout
12 the year, is really an important factor to a quality
13 review. Also, it helps the concurring partner get
14 their head in the game, which is critically important,
15 particularly in complex work.

16 I certainly understand the board's desire
17 not to be too prescriptive about timing. I appreciate
18 that timing, best timing practices differ dramatically
19 from job to job. But I am surprised that it almost --
20 it walks away from the issue and abdicates any counsel
21 in a standard in what, in my experience, has been
22 mission critical to a quality concurring partner
23 review.

1 JENNIFER RAND: Greg, can I just ask you to
2 expand on what you might think would be appropriate to
3 include, recognizing the standard would be to be
4 applied for all public company audits to have an
5 engagement quality review? So kind of what in your
6 view in the timing would you like to see mentioned, if
7 you have any more thoughts specifically?

8 GREGORY JONAS: Well, if the document at
9 least talked about the importance of timing, the
10 importance of concurring partners to get in early,
11 where desirable, the advantages of doing this, and
12 simply observe that one of the factors that one
13 considers when deciding whether a concurring review
14 was substantive in part relates to the timing. I
15 wasn't thinking more than that.

16 JENNIFER RAND: Thank you.

17 GREG SCATES: Liz Fender.

18 ELIZABETH FENDER: I'm not sure I'm reading
19 it correctly, but I was questioning the differences
20 between the procedures required for an interim review
21 versus an annual review, and I think the wording was
22 trying to make it clear that if you're doing an
23 interim review, you don't have to look at the prior

1 year's disclosures about internal control for the
2 annual review report. One, is that correct? And two,
3 would you really do that? Would you really review
4 somebody's interims and not take a look at what
5 somebody raised in the prior annual review?

6 GREG SCATES: Liz, are you talking about the
7 prior -- a review of a prior quarter, or are you
8 talking about the annual audit?

9 ELIZABETH FENDER: I think the wording says
10 you only have to look at the prior interim
11 information. So I didn't know if that was meant to
12 say you don't have to look at the prior year's annual
13 audit reports.

14 GREG SCATES: Well, the engagement quality
15 reviewer would be looking at it if he or she is not
16 already familiar with the engagement and what happened
17 in the prior year's audit. If he or she was new to
18 the engagement, then they would obviously look at
19 prior year's audit and see what the issues were, what
20 the audit issues were. In carrying out the interim
21 review, they would look at the prior quarter. If
22 there's a prior quarter they looked at, then they
23 would look at that to see what the issues are, because

1 they want to keep current with the issues and know
2 what they are going into that review.

3 ELIZABETH FENDER: I agree with the
4 sentiment. I'm just not sure the words are clear
5 about that. But obviously, you do have to familiarize
6 yourself with the engagement. But when it was trying
7 to describe the differences between what you're
8 required to do in an interim versus an annual, it sort
9 of said you only have to look at the prior interim.

10 GREG SCATES: Okay. We'll look at that and
11 make sure that's clearer. Thank you.

12 Doug Anderson?

13 DOUGLAS ANDERSON: I had a concern on how
14 the objective is worded and how the procedures in
15 Paragraph 10 and Paragraph 9 are described. As I read
16 the objective, which I think is a great idea to have a
17 clearly stated objective for the standard in Paragraph
18 2, it seems pretty broad. It looks like we want to
19 make sure that there's a good evaluation of judgment,
20 a good evaluation of conclusions received. As I look
21 at Paragraph 10, it talks about, in Part B, that the
22 reviewer should evaluate the risk assessments, the
23 audit responses, the scope of the work. Those all

1 seem pretty broad. As I go back up, though, to
2 Paragraph 9, it says you're supposed to do that merely
3 by holding discussions with the engagement team,
4 effectively, in reviewing documentation.

5 Those, to me, seem to be inconsistent. The
6 objective and what we're trying to get out of this
7 review seem very broad and comprehensive, but then
8 we've limited the procedures, and my concern is those
9 two things could be considered in conflict, that the
10 external auditing firms will then revert back to what
11 they think the objective is driving as opposed to what
12 Paragraph 9 is saying.

13 So as I look at this, it just seems
14 inconsistent, those two directions in the standard
15 looking consistent, and either needing more
16 clarification back up in Paragraph 2 as to what the
17 objective is, or maybe more clarification in 10(b)
18 about that.

19 GREG SCATES: Thank you, Doug. We'll take
20 another look at that and make sure that they are
21 consistent and clear and concise.

22 Bob Dacey?

23 ROBERT DACEY: Thanks, Greg. We, too,

1 appreciate the changes that were made in response to
2 the comments on the earlier draft but still have some
3 concerns about -- at least it's our perception that
4 some of the other standards, particularly the IAASB,
5 are at a more general principle level than what this
6 would provide in the PCAOB. And again, in this area
7 as well as other areas, we just have the concern as to
8 whether or not there's a perception that the general
9 principle stated in some of these other standards are
10 consistent with where you are going or different
11 because of the different terminology that you're
12 using.

13 So we just want to, again, raise that point
14 of concern in this area in particular as to whether or
15 not that will create any conflict in application.

16 Thanks.

17 GREG SCATES: Hal Schroeder?

18 HAROLD SCHROEDER: Echoing some comments
19 that were made earlier, I am curious myself as to why
20 LISI, signing off on the engagement planning portion,
21 it's not encouraged or recommended that it's done
22 concurrent at the same time the partner has signed off
23 on it. The reviewing partner should be signing off on

1 the planning before anything substantive is done,
2 because as I read through the requirements, you don't
3 have any opportunity to make any recommendations or
4 changes. The game is over by the time you get
5 involved, and I would strongly recommend that at least
6 there be two segments to a reviewer's involvement,
7 early in the process, and then at the end of the
8 process.

9 GREG SCATES: Thank you, Hal.

10 Kurt Schact?

11 KURT SCHACT: A quick question for those of
12 us not in the profession. I'm curious how often does
13 the EQR result in a material change, and does the
14 PCAOB, or should it, keep statistics on that so that
15 you have some statistical evidence of how often
16 problems should be found in a particular company's
17 audits?

18 GREG SCATES: You can look at some of our --
19 our inspection reports have cited some findings with
20 respect to the performance or lack of performance,
21 aggregate performance in the engagement quality
22 review, but we don't have any statistics on it. But
23 I'd be interested in hearing from the profession,

1 anyone that wants to.

2 Vin Colman?

3 VINCENT COLMAN: I'll certainly be brief.

4 That kind of statistic would be very difficult if your
5 objective is a good engagement quality review. I do
6 engagement quality reviews now, and to say did you
7 catch something, if you're doing it well from the
8 planning through the execution to the final and you
9 are engaged with the engagement team, you're both
10 independent, but yet you're understanding issues as
11 they arise. So the objective is to avoid looking for
12 the statistic that you're asking for, because the
13 objective is to get it right before you even would get
14 into that position, if you're doing your job right,
15 correctly.

16 GREG SCATES: Paul Sobel?

17 PAUL SOBEL: Thinking through the 302
18 disclosure requirements, I do see -- and I'm thinking
19 of interim reviews. I think it was covered well for
20 the annual review. There is mention about changes.
21 Presumably that's material changes and internal
22 control over financial reporting. I didn't see any
23 specific mention about any frauds that might be

1 identified, committed by management or those involved
2 in the financial reporting process. Is that just
3 considered to be intuitively covered by one of the
4 other items?

5 GREG SCATES: Paul, can you explain that --
6 can you go over that discussion again? I'm not sure I
7 understand what you were saying.

8 PAUL SOBEL: Okay. If there is an incident
9 of fraud committed by a member of management or those
10 integrally involved in the financial reporting
11 process, it has to be disclosed to the audit committee
12 and the independent outside auditor. I presume, even
13 with interim financial statements, that might raise
14 questions by the engagement partner, and I wasn't sure
15 how that would be covered, then, in the EQR in terms
16 of the resolution or conclusions about the impact such
17 a fraud may have on the interim information.

18 GREG SCATES: The auditor is clearly under
19 an obligation, a professional obligation, that if
20 something comes to their attention, that they have to
21 resolve it. They cannot have some information before
22 them and because it has serious consequences with
23 respect to not only the interim financial statements

1 but also the annual, so they have to resolve any
2 particular issue that might be a fraud indicator.

3 PAUL SOBEL: I understand that, and I guess
4 my question was, as I say, it may be subsumed in one
5 of these bullet points, is how does the concurring
6 partner get comfortable with the conclusions of the
7 engagement team with regards to that resolution?

8 GREG SCATES: Well, the engagement quality
9 reviewer would have to use his or her professional
10 judgment, and that's what that individual's duty is,
11 is to challenge what the team has done. So he or she
12 would be challenging the team's conclusion on any
13 matter, whether it's a matter that you brought up or
14 any other matter.

15 Any audit or accounting issue that they are
16 confronted with, that person is charged with that and
17 has that obligation to make sure that they are
18 concurring with the resolution, because if they're
19 not, then they need to have a further discussion.
20 They may have to -- he or she may have to have
21 additional evidence before he or she concurs.

22 PAUL SOBEL: Yes, I understand that side.
23 I'm either way off base or not making myself clear. I

1 understand what the process should be. The interim
2 procedures are silent with regards to that. So what
3 I'm hearing you saying is that that would just go
4 along with any of the other judgments, material
5 judgments that are made and doesn't need to be
6 specifically identified as something that should be on
7 the radar screen of the concurring partner, because
8 again, material changes and internal control are
9 mentioned as one of the items, but fraud is not.

10 GREG SCATES: Okay. Well, we'll take
11 another look at that.

12 JENNIFER RAND: Paul, I see fraud mentioned
13 in Paragraph 15 regarding interim. I don't know, it's
14 one of the -- under 15(a). "Engagement quality
15 reviewer should evaluate the nature of identified risk
16 and material misstatement due to fraud." Does that --

17 PAUL SOBEL: It may. I saw that particular
18 point, and to me that was more forward looking, what
19 are the risks, what are the potentials, and I was
20 referring to something that was known and identified.

21 GREG SCATES: Gary Kabureck?

22 GARY KABURECK: Thank you. This question I
23 thought of when Kurt had raised his question about

1 tracking statistics, if you will, when the engagement
2 reviewer overrules the -- excuse me -- the quality
3 reviewer overrules the engagement partner.

4 My question: Did the board consider, or
5 should you consider if you didn't, if there really is
6 a significant override by the concurring partner and a
7 decision is changed, whether it's audit scope or
8 accounting or disclosure decisions, should there be a
9 requirement for communication with the audit
10 committee, or at least the audit committee chairman,
11 of that event?

12 Again, I appreciate a lot of this stuff.
13 We'll eventually agree, and eventually we'll get the
14 evidence, but there's going to be times, presumably
15 when the engagement team is overruled on something
16 that's important, and from a client service point of
17 view, should there be a requirement for at least the
18 audit committee or the audit committee chairman to be
19 advised of that? I don't know if that's -- I don't
20 know if you considered it and rejected it. I'm not
21 even suggesting that that should be the answer, but I
22 think it should be considered.

23 GREG SCATES: So any instance, then, you're

1 saying, in which the engagement team arrived at a
2 conclusion and then the engagement quality reviewer
3 would disagree, and then the ultimate conclusion is in
4 the favor of the way the engagement quality reviewer
5 wanted to go, so he or she overrides what the
6 engagement team did?

7 GARY KABURECK: Yes, correct. And
8 presumably, anything they would override them on would
9 be something material to the engagement, whether it's
10 on the audit scope or an accounting conclusion,
11 because this is supposed to be risk focused. Again,
12 I'm not saying that should be the answer, to advise
13 the audit committee or the committee chair. I'm just
14 asking did you consider it, and if you didn't, maybe
15 you could before you finalize it.

16 GREG SCATES: Would anyone else like to
17 weigh in on that? Yes, Gaylen Hansen?

18 GAYLEN HANSEN: I would be very cautious
19 about using the word "override." We -- I think
20 ultimately the engagement partner has to be
21 responsible for the opinion that is issued. He's the
22 final person on the line there, but that doesn't mean
23 to say that that engagement quality reviewer, the

1 concurring reviewer, doesn't take that further to the
2 firm's quality control partner, to the director of
3 audit services, whatever the structure is within that
4 firm to try to get resolution.

5 But I think that resolution aspect is a
6 little bit lacking in the standard. But I'm a little
7 bit antsy about this idea that one person can override
8 another person in its entirety.

9 GREG SCATES: Thank you, Gaylen, and thank
10 you, Gary.

11 Wayne? Wayne Kolins?

12 WAYNE KOLINS: On that point, I would also
13 be cautious, and even if the word "override" is not
14 used and it's a different word, like maybe if there's
15 a disagreement and the engagement quality reviewer's
16 position is the ultimate position, then you'd have to
17 get involved with defining disagreements again, which
18 is now in the literature between the issuer and the
19 audit firm, and there's a whole different reason for
20 that in terms of the pressure that might be put to
21 bear, which I don't think exists on the engagement
22 team.

23 I'd also be concerned about, in terms of

1 considering this, what that would do to the mindset of
2 the engagement partner in helping to resolve this
3 disagreement. It may make the engagement partner more
4 obstinate in terms of the resolution.

5 GREG SCATES: Jim Cox? Oh, I'm sorry.
6 Jamie Miller. Sorry.

7 JAMIE MILLER: I think Gary's point is a
8 good one, and it's really a question to me as to how
9 the governance structure works between the auditor and
10 the preparer. I think the key question is how to
11 determine what would get communicated, and I think
12 perhaps one way to think about it would be to consider
13 whether audit committee communication would be
14 required in situations where a formal resolution
15 process had to be invoked to resolve the disagreement,
16 as opposed to those matters that are resolved in the
17 normal course, through additional audit procedures or
18 additional discussion between the concurring review
19 partner and the audit partner. But I think it is
20 something that ought to receive some level of debate.

21 GREG SCATES: Thank you, Jamie.

22 Jim Cox?

23 JAMES COX: I'm sort of struck by the

1 opacity of the second paragraph. It states the
2 objective. And I think if we had less opacity, we
3 would deal with a lot of questions which were started
4 off by Harold's comment about what we really want to
5 have happen here.

6 You can think of a wide range of objectives
7 that could be served within this language, and I think
8 we ought to specify which one of it is we want. One
9 would be make this year's audit better. Another one
10 would be make next year's audit better. A third one
11 could possibly be an internal evaluation of your own
12 staff doing this. A fourth one could be an external
13 evaluation by the audit committee.

14 I mean, what exactly is the objective of the
15 external quality review? I think if you come to grips
16 with that, many of these questions on this session
17 would shake out from that. But currently, I think
18 that, again, just to repeat myself here, I'm struck by
19 what I perceive as the opacity of the second paragraph
20 stating what the objectives are. I think it's fairly
21 -- it's too generalized to be very helpful to somebody
22 who is going to have to govern their conduct as an
23 external reviewer, or what to make of the external

1 review going forward.

2 GREG SCATES: Thank you, Jim.

3 Joe Carcello?

4 JOSEPH CARCELLO: As some of you know, I've
5 spent a lot of time over the years working with
6 accounting and auditing enforcement releases, and one
7 of the things we've seen in some of those, certainly
8 not the majority but in some situations where
9 obviously there is ultimately a fraud, and people
10 lower on the engagement team had come across issues
11 that were problematic and were dissuaded from being
12 overly concerned about those issues by people higher
13 on the engagement team. And so my concern ties into
14 Paragraph 9, where the last sentence in that paragraph
15 talks about holding discussions with the person with
16 overall responsibility for the engagement, holding
17 discussions with other members of the engagement team,
18 as necessary.

19 I guess I would encourage the board to at
20 least think about eliminating the words "as
21 necessary." In today's world, with the ubiquity of
22 cell phones, you would not have to have this
23 discussion face to face. By the time the second

1 partner review is happening, often members of the
2 engagement team are on to the next job. But you could
3 easily pick up a cell phone and just touch base with
4 everybody on the engagement team to just make sure
5 there wasn't an issue that really troubled them, that
6 they maybe were dissuaded from pushing too hard by
7 others higher up in the chain.

8 GREG SCATES: Thank you, Joe.

9 Bob Dacey?

10 ROBERT DACEY: I just wanted to add a point.

11 In terms of our government auditing standards, we
12 wanted to clarify in our latest release that, in fact,
13 the firm ought to have procedures in evaluating or
14 monitoring the quality review process, both in terms
15 of identifying any systemic issues that were
16 identified through quality reviews, as well as where
17 the quality review function is being carried out
18 properly in terms of a monitoring procedure.

19 So I'd just offer that in terms of what
20 we've also addressed to deal with the issues of
21 differences and whether or not things caught in a
22 quality review, how they were dealt with, and again
23 whether that's a systemic issue in the firm.

1 GREG SCATES: Greg Jonas?

2 GREGORY JONAS: Greg, I'm about to betray my
3 ignorance, so apologies in advance. Does the new
4 quality control requirement apply to review of work
5 supporting the 404 report on internal control?

6 GREG SCATES: Yes.

7 GREGORY JONAS: And that is quite a change
8 in practice relative to current practice or concurring
9 partner reviewers?

10 GREG SCATES: No. They currently perform
11 that review of the internal control as well as the
12 audited financial statements.

13 GREGORY JONAS: Is it worth making crystal
14 clear in the final document that if the auditor has an
15 integrated audit, that these requirements apply to
16 that 404 work as well, or was I the only person in the
17 room who was left wondering whether it does or
18 doesn't?

19 GREG SCATES: Well, I'll go back and look at
20 it again. I thought it was clear, but maybe -- we'll
21 make sure it is.

22 GREGORY JONAS: It could be my fault. It
23 very well could be my fault. Thank you.

1 GREG SCATES: That's fine.

2 Jeff Mahoney?

3 JEFF MAHONEY: I just wanted to follow up on
4 Kurt's question earlier, and Professor Cox's comments
5 about the objective. In connection with the PCAOB's
6 inspection process, have you identified any issues or
7 concerns regarding the EQR process, and can you tell
8 me what two or three of the main issues or concerns
9 were?

10 GREG SCATES: One of the issues is apparent
11 when you look at some of the inspection reports. The
12 question that presents itself is once you see the
13 deficiencies that are identified, then you obviously
14 ask yourself why didn't the engagement quality
15 reviewer detect some of these deficiencies. I mean,
16 that's paramount. With not all the inspection
17 findings but some of them, you'll see that, and we
18 make that clear in some of the reports.

19 Another issue that comes up is the
20 documentation of the engagement quality review
21 process. We have noted that in the reports that it's
22 not sufficient to indicate what the person did and
23 what the person reviewed and what conclusion they

1 arrived at, because it's hard to tell if they did
2 anything at all. So those are just a couple of
3 findings I would note.

4 Any other comments on the engagement -- yes,
5 Tom?

6 THOMAS TEFFT: I've just given some more
7 thought to the question about whether there should be
8 a requirement for communication to the audit committee
9 if there's disagreements or, again, I understand the
10 word "override" is probably a little inflammatory, but
11 for lack of a better word right now.

12 I just think you'd need to really consider
13 what the objective of that communication would be
14 because, as I think more about it, if an auditor in a
15 firm is carrying out the work outlined in the
16 standards such that the reviewing individual can issue
17 the concurring report, then from an audit committee
18 standpoint, the audit committee should be satisfied
19 that the work was done and not be concerned about the
20 inner workings within the audit firm that led to that
21 conclusion.

22 Not any different than for a preparer if
23 there are debates and dialogues within a company as

1 it's preparing its financial statements. I just think
2 to the extent the board considers a requirement, you
3 would be very explicit as to what the objective would
4 be because, otherwise, you could get into a very
5 inefficient process and a very slippery slope there in
6 terms of what's coming back to the audit committee.

7 GREG SCATES: Gaylen Hansen?

8 GAYLEN HANSEN: Just following up a little
9 bit on that, in that respect, I wonder to what extent
10 the board considered the interaction of the concurring
11 reviewer with the client itself? And this has come up
12 from time to time. Do they have the same level of
13 discussion access as the engagement partner? Do they
14 meet as regularly? Do they meet in person? Do they
15 call independently? To what level is that
16 independence of the concurring reviewer?

17 I've seen this done both ways, where the
18 firm wants as much insulation and independence as
19 possible of the reviewer, and others that say, well,
20 if they know the client better, they'll understand
21 where they're coming from and so forth. But to what
22 extent was that considered?

23 GREG SCATES: We did have some discussions

1 of that, particularly with respect for the engagement
2 quality reviewer to maintain his or her objectivity.

3 And one of the issues, obviously, has to do
4 with when you do have some accounting and auditing
5 issues or contentious issues that come up, but most
6 importantly here is that the engagement team has
7 identified the issue. They gathered the evidence, and
8 they've come to a conclusion. At that time, then the
9 engagement quality reviewer, it would be appropriate
10 for him or her to step in and take a look at it.

11 But most importantly here is that the
12 engagement quality reviewer cannot be a part of the
13 initial process of gathering the facts and gathering
14 the evidence. That's not their job. And they need to
15 stay outside and look in when the issue has been --
16 when the team has come to an initial conclusion. Then
17 it's appropriate for that person to come and step in
18 and take a look at it.

19 So objectivity here is very important
20 because this person does not play -- is not going to
21 fill the shoes of the engagement partner. And so,
22 it's very important -- it was very important to the
23 staff when we were developing and drafting the

1 standard to make sure that this person stays outside
2 and looks in and maintains that objectivity.

3 JENNIFER RAND: Gaylen, as just to kind of
4 follow up, I'd be interested if you have any
5 experiences at your firm or other firms kind of
6 regarding the engagement quality reviewer's
7 communications with the client or preparers have any
8 observations on how things are handled, that
9 experience and how that's been helpful or not helpful?

10 GAYLEN HANSEN: I think some level of
11 insular or compartmentalization of that individual
12 makes some sense to at least consider that, and we
13 kind of do that within our firm. We don't want that
14 individual calling the CFO and having these
15 discussions independently. We think that should go
16 through the engagement partner, except for when
17 they're involved in, say, an audit committee meeting.

18 GREG SCATES: Thank you, Gaylen.

19 Sam Ranzilla?

20 SAM RANZILLA: Well, having listened to the
21 better part of the last 20 minutes, just a couple of
22 observations. One, I think it's important that we
23 keep in mind the objective, and then I understand some

1 think that the standard could be improved. And I
2 don't know that I disagree with that.

3 But the objective here is to improve audit
4 quality and improve financial reporting, and having --
5 I hear sort of a sentiment around turning the
6 engagement quality control reviewer into another
7 policeman where statistics are kept on what they found
8 or communications made to the audit committee about
9 where they overrode somebody. I don't think that's
10 actually going to improve the situation.

11 From the perspective that the engagement
12 quality review is just one element of the firm's
13 overall system of quality control, and there are
14 plenty of policemen at the firms with respect to
15 internal inspections and other parts of the quality
16 control system where there is a vetting and a "second-
17 guessing" of that engagement partner, I think this
18 role should be more in line with getting it right the
19 first time, improving the quality of audit, and that
20 client's financial reporting and communication to
21 investors.

22 So I think it's a balancing act. I just --
23 I caution you against turning this role more into a

1 policeman than what would be appropriate.

2 GREG SCATES: Thank you, Sam.

3 Any other comments on the engagement quality
4 review process?

5 VINCENT COLMAN: You know, I do want to
6 follow up on I guess Sam and Gaylen's point. I do
7 think you need to strike the right balance between
8 objectivity and independence that you do already have
9 in the standard.

10 But to do engagement quality, to get it
11 right the first time, as Sam just said, there does
12 need to be a certain level of interaction to make sure
13 that you have a deep enough understanding of what
14 those critical decisions and issues are. And if you
15 go too far away, as I think that was just suggested,
16 perhaps you cannot get it right the first time, and
17 that's the objective.

18 GREG SCATES: Thank you, Vin.

19 Larry Salva?

20 LAWRENCE SALVA: Thanks. Two points. I
21 guess on the interaction with the concurring partner -
22 - between the concurring partner and the client
23 interaction, I think the firms may take different

1 approaches and at times may have taken different
2 approaches as to how much exposure concurring partners
3 were giving to clients. I think that can really be
4 left up to them in terms of what works best.

5 My current experience that I do with the
6 firm that I'm working with now, there was a point in
7 time that I knew the name of the concurring partner
8 but had no interaction with the concurring partner at
9 all. And more recently, I've had some interaction,
10 but limited. And I don't think engagement quality has
11 suffered in either of those cases. It's an internal
12 working for the firm in terms of what works best for
13 them.

14 The other point I'd make is in terms of
15 communication with the audit committee. If that is
16 considered by the board, I think it should stay out of
17 this standard. There is a whole slew of things that
18 should get communicated to audit committees, and I
19 think about the audit committee communication that I
20 have in terms of kind of a standard question from my
21 audit committee chair is what close calls may have
22 been debated within our disclosure committee, our
23 internal management committee that discusses issues

1 and resolution?

2 And if the audit committee chair is so
3 inclined to ask the engagement partner or the
4 engagement team were there issues that were resolved
5 through involvement of the engagement quality reviewer
6 that would have been resolved differently had that
7 review not occurred, fine. Let the audit committee
8 chair be interested in that or put that into the mix
9 of all of the communications that the auditor should
10 have with the audit committee.

11 But I think it should stay out of the
12 specific standard. It shouldn't be called out as a
13 requirement here.

14 GREG SCATES: Okay. Thank you, Larry.

15 Any other comments on this particular topic,
16 on the engagement quality review process?

17 [No Response.]

18 GREG SCATES: Okay, let's turn to the next
19 topic, to the concurring approval of issuance. The
20 original proposal provided that the reviewer must not
21 provide concurring approval of issuance if he or she
22 knows or should know, based upon the requirements of
23 the standard, of certain engagement deficiencies.

1 In response to concerns expressed by
2 commenters, the board revised this provision so that
3 it relies instead on the auditor's existing duty to
4 exercise due professional care rather than using the
5 phrase "knows or should know, based on the
6 requirements of the standard."

7 Like the formulation in the original
8 proposal, the revised provision makes clear that a
9 reviewer cannot evade responsibility because as a
10 result of an inadequate review, he or she did not
11 discover a problem that a reasonably careful and
12 diligent review, a review performed with due
13 professional care, would have revealed.

14 For our discussion this morning, let's
15 discuss the questions from the release that addressed
16 concurring approval of issuance. In front of you on
17 the screen is the standard for the engagement quality
18 reviewer's concurring approval of issuance
19 appropriately described in the repropoed standard.
20 Is the first edition appropriately tailored to reflect
21 the difference in scope between an audit and an
22 interim review?

23 Jim Schnurr?

1 JAMES SCHNURR: Thank you.

2 We viewed the removal of "know and should
3 know" as a positive step but are a little bit confused
4 by the fact that in the discussion in the fore part of
5 the standard, they define "due professional care" as
6 the same as "know or should know." So it seemed to me
7 that while in one instance, they changed the language,
8 they made it clear that they thought the standard was
9 still the same. And I don't think that addresses the
10 concerns that we and others have expressed around
11 that.

12 The second point I would make is it seems
13 odd to me that an individual auditing standard would
14 specifically point out a requirement for due
15 professional care when there is an overall standard,
16 auditing standard that deals with due professional
17 care, which applies to all standards. And so, it
18 seems very odd to me that we would have a separate
19 standard, which is then if you want to call it
20 somewhat defined in the fore part of the standard.

21 GREG SCATES: Other comments? Gary?

22 GARY KABURECK: Picking up where Jim was
23 just talking, looking at the way at least I read,

1 whether it's auditing releases or accounting
2 standards, there is the standard, and then there is
3 the backup material, in this case the release, you
4 know, the basis of conclusions and FASBs.

5 So usually the standards are pretty clear in
6 what they say, accounting or auditing or whatever.
7 Then you go, "What do you mean?" I mean, you tend to
8 go to the releases and the issuing cover memos and
9 stuff where you get a little bit more free form in the
10 words. And I mean, I've found over 25 years or so is
11 those are often more useful in terms of communicating
12 intent than the final standard itself.

13 So I can empathize where what Jim is saying
14 with as a preparer, it doesn't matter all that much to
15 me. The preparers, I think, when they commented,
16 worried about does this become a second audit? I
17 think you were trying to address that, but I can see
18 where they would read that there's a conflict between
19 the release and the standard. Maybe they're reading
20 it wrong. Maybe it's unintentional. Maybe it's just
21 a draft -- choice of words and drafting.

22 But seriously, the covering documents' basic
23 conclusion stuff get read very heavily on any

1 assessment or interpretation of standards.

2 GREG SCATES: Other comments on concurring
3 approval of issuance? Okay --

4 GAYLEN HANSEN: Greg, I think it's a great
5 idea.

6 [Laughter.]

7 GAYLEN HANSEN: I think it should happen.
8 So --

9 JENNIFER RAND: So you're supportive of it?
10 This is an area we did receive a lot of comments. So
11 interested in views in what we've done.

12 Gaylen, I thought I heard you say --

13 GAYLEN HANSEN: Yes, I mean, I think it all
14 ties back into the timeliness that we've had of prior
15 discussion about whether they're involved or whether
16 this review is taking some -- is being wrapped up, and
17 there are points that are open after the filing has
18 been made.

19 I just can't imagine that there wouldn't be
20 some level of formal signoff on the concurring review.
21 And after the fact doesn't do anybody any good.
22 Unless you're talking about next year's audit, Jim.

23 GREG SCATES: Vin Colman?

1 VINCENT COLMAN: Yes, I just wanted to
2 reiterate. You don't want to repeat, but I also don't
3 want the silence in this room to make the point that
4 Jim and Gary have just made, that it's not a
5 significant point.

6 I mean, you've got -- I think that the
7 standard from a year ago has been significantly
8 improved, as Randy said, and really appreciate that.
9 But by far, this was the biggest issue with respect to
10 the "known or should have known." And it seems that
11 it's been taken out of the standard, but yet used as a
12 synonym to "due professional care."

13 There is another standard that's out there
14 on due professional care. I think we know what it is.
15 And then to have something in there that basically
16 almost redefines "due professional care" to be "known
17 or should have known," I really question whether or
18 not you address the issue. And it's now done in a
19 way, as Gary pointed out, it's in the back somewhere.

20 I'm not sure it was a drafting error. Is
21 that what we are saying or not? And I'm a little bit
22 concerned, did we address it or not? I think we all
23 felt like we did, but yet when you really read it, the

1 answer is maybe we didn't. And I think it does need
2 to be addressed. As was discussed many, many times
3 with the unintended consequences if you were to go in
4 that direction, there's a real concern around it.

5 GREG SCATES: Thank you, Vin.

6 Doug Anderson?

7 DOUGLAS ANDERSON: Not to pile on, but just
8 to emphasize a point that I was trying to make
9 earlier. This whole issue of "known or should have
10 known," when you marry that together with the
11 objective that's very broad, I don't know how it's
12 possible to accomplish that objective, especially the
13 standard of "known or should have known" based on what
14 it says in paragraph 9. And I get back to that's why
15 I think the standard is inconsistent.

16 It holds the auditor to a high level of
17 performance but then says you're only supposed to do
18 that with these limited steps. And I worry that the
19 objective and the expectation far exceeds what we're
20 saying they're supposed to do, and that's the primary
21 conflict I see in the standard.

22 You put the external auditor in a very
23 difficult situation of holding him to a high result,

1 but saying they have to get there by doing limited
2 procedures. And if that comes to fore, I think the
3 objective will win out over what paragraph 9 says.

4 GREG SCATES: Other comments before we leave
5 this area? Any other comments? Paul Beswick, SEC.

6 PAUL BESWICK: Well, Greg, I think it would
7 be helpful if the staff did provide some views to the
8 questions that Vin and Jim and others have raised as
9 through the release, have you redefined "due
10 professional care," or are we relying on the existing
11 standard?

12 It seems to be a question that was posed,
13 and I think it would be helpful to people who are
14 providing comments if there is some clarification
15 provided.

16 GREG SCATES: Any other comments?

17 [No Response.]

18 GREG SCATES: Okay, let's move to the last
19 topic for discussion with respect to engagement
20 quality review. Let's talk about the documentation I
21 alluded to earlier.

22 Under the new proposal, documentation of the
23 engagement quality review should contain sufficient

1 information to identify who performed the review, the
2 documents reviewed, and significant discussions held
3 during the review and the date that the reviewer
4 provided concurring approval of issuance.

5 If the reviewer did not provide concurring
6 approval of issuance, the proposal would require
7 documentation of the reviewer's reasons for not
8 providing concurring approval of issuance. The final
9 question then states before you on the slide, are the
10 documentation requirements in the repropoed standard
11 appropriate? If not, how should they be changed?

12 Gaylen Hansen?

13 GAYLEN HANSEN: Paragraph 19 says, "If no
14 concurring approval of issuance is provided, the
15 reasons for not providing the approval need to be
16 documented." And maybe you can help me out with this,
17 but if the review is required in order to be issued in
18 accordance with paragraphs 12 and 13, I don't know --
19 it seems contradictory.

20 How can you issue the financial statements
21 without the review? But if you don't have the review,
22 you have to document why you didn't have the review?
23 It just seems a little bit strange.

1 GREG SCATES: You are correct. I mean,
2 obviously, Gaylen, if there is no concurring approval
3 of issuance, then the firm cannot issue the report.
4 You're right. We thought you should just close the
5 gap and explain what happened, and the work papers can
6 be -- because the report may never be issued. The
7 work papers can be archived as is.

8 Then you can plead there may have been some
9 discussion. I'm sure there were a lot of discussions,
10 but the concurring partner or the engagement quality
11 reviewer can close the gap, can close down what he or
12 she was responsible for, here's what happened, and
13 then they're finished. They're complete.

14 But you're right. You're right. There is
15 obviously not going to be a report issued until there
16 is an engagement quality review performed and they
17 concur.

18 Jim Schnurr?

19 JAMES SCHNURR: In looking at the
20 documentation in 19(c), which requires the reviewer to
21 document discussions with the engagement team,
22 significant discussions, going back to some of the
23 comments we had earlier about Vin's comments around

1 the process or the interaction between the reviewer
2 and the engagement team, I don't see -- and Sam's
3 comments earlier about what the objective is here. I
4 don't see how the documentation improves audit
5 quality.

6 The engagement team has already documented
7 in the work papers their conclusions about whatever
8 the particular either financial reporting or auditing
9 issue was. So this looks more like, as Sam talked,
10 police or a cop coming in and having to document the
11 discussions. It doesn't seem to add to audit quality,
12 and it seems to be -- I'm not sure what the purpose of
13 it is. It's not really described as to what the
14 purpose of that is.

15 So I don't see any incremental benefit, and
16 it would potentially add a lot of time to the process.

17 GREG SCATES: Jim, looking at it from the
18 perspective of let's look at the engagement team
19 first. But doesn't documentation, hard documentation
20 drive good audit quality?

21 JAMES SCHNURR: I agree with that, but the
22 engagement team under the auditing standards already
23 has a requirement to document their significant

1 conclusions. And what we're asking the reviewer to do
2 is simply concur on those conclusions.

3 So I don't know why that the reviewer would
4 then have to document in the detail that seems to be
5 here their discussions with the engagement team. I
6 mean, there is already the overall requirement that in
7 terms of issuing the report, he essentially or she has
8 to be comfortable with those conclusions before they
9 give their approval.

10 So an incremental documentation -- and given
11 the number of discussions that potentially are held, I
12 mean, if you think of a large multinational
13 engagement, concurring reviewer may spend hundreds of
14 hours on that engagement. If they have to document
15 every time they have a conversation around a
16 significant judgment, again, it's unwieldy, and I
17 don't see the benefit to the overall audit quality.

18 GREG SCATES: Sam Ranzilla?

19 SAM RANZILLA: I totally agree with Jim, and
20 the only point that I will add is looking at the
21 purpose of that -- what I might envision to be the
22 purpose of adding that requirement based on the
23 proposing release. That requirement almost looks to

1 me like an inspection, that that requirement is
2 focused on your inspection process.

3 And I can appreciate that, but again, I
4 would caution the board on writing auditing standards
5 in order to improve their ability to inspect auditors.

6 GREG SCATES: Thank you, Sam.

7 Joe Carcello?

8 JOSEPH CARCELLO: Greg, if you forgive me, I
9 want to go back and revisit the last discussion
10 briefly. I'm sorry I didn't comment on it, but I
11 needed a little bit of time to formulate my thoughts.

12 My friends in the profession express a lot
13 of concern about this due care issue and as it ties
14 into "know or should have known." And so, maybe
15 there's an issue there that I don't fully understand,
16 and if there is, I'd like them to articulate it.

17 But I guess from an investor perspective, to
18 me, the way that that standard -- the proposed
19 standard is written is essentially it says if you
20 review the documentation that the standard requires
21 you to review, if you have the discussions that the
22 standard requires you to have, using due care, which
23 includes professional skepticism, then if there is a

1 problem that's obvious from doing that, you either
2 know it, but you can't know someone's state of mind.
3 Or you should have known it, which allows for the fact
4 that you can't know someone's state of mind.

5 And I'll give an example of why I think this
6 is important. I've done some expert witness work for
7 the Securities and Exchange Commission. And in one of
8 the cases that I did, they were seriously thinking
9 about bringing an enforcement action against the
10 second partner, and they decided not to bring the
11 enforcement action because the existing standard was
12 sufficiently vague that they felt that they didn't
13 have a strong enough legal basis to bring that action.

14 But I would give you kind of a concrete
15 example. Let's assume I'm the second partner on an
16 engagement, and in the work papers, inventory
17 obsolescence is an issue. And so, I look at the
18 documentation, and the documentation is a client
19 schedule of a high and low estimate of the
20 obsolescence reserve that is X'd through with no
21 explanation, substituted with another client schedule
22 with a high and low estimate, which are much lower
23 numbers than on the first schedule.

1 And the number that's picked and that ends
2 up in the 10-K is the low number, which is the same
3 number that was in the 10-K in the previous year,
4 where inventory had increased by a factor of 3 or 4 or
5 5 and with indication that inventory was not turning
6 over at all.

7 To me, that would indicate that if I'm the
8 second partner and the audit procedures that had been
9 done were minimal, at least in terms of documentation
10 of those audit procedures, to me, that would indicate
11 that I know or, if I didn't know, I should have known
12 that I probably don't have sufficient appropriate
13 audit evidence as it relates to the inventory
14 obsolescence reserve because if I had used due care or
15 professional skepticism, I would be troubled by that.

16 So maybe there's a legal issue that the
17 people in the firms can explain to me. But short of
18 that, it seems to me that the PCAOB's language here is
19 completely appropriate.

20 GREG SCATES: Thank you, Joe.

21 Doug Anderson?

22 DOUGLAS ANDERSON: To go back to the other
23 topic on documentation, I tend to agree with Jim that

1 I see 19(c) as unnecessary. If you've got the
2 paragraph 16 and you've got the recurring partner
3 completing 19(a), (b), and (d), I don't know what
4 19(c) adds.

5 GREG SCATES: Jeff Mahoney?

6 JEFF MAHONEY: Thank you.

7 I'm certainly not supportive on unwieldy,
8 unnecessary documentation, but you said to me a few
9 minutes earlier that your inspection results revealed
10 a lack of documentation so that you're unable to
11 determine what the reviewer actually did. So I would
12 err on the side of having more documentation, not
13 less.

14 GREG SCATES: Thank you, Jeff.

15 Hal Schroeder?

16 HAROLD SCHROEDER: I would agree and take
17 the opposite side of Doug. It's been a few years
18 since I've done an audit, but when we had a concurring
19 partner involved, we always -- the audit team would
20 write up that discussion and what the conclusions
21 were. So all the independent partner or engagement
22 reviewer, whatever we're calling it today, would come
23 in and sign off on that memo.

1 So it would be not a tremendous burden, but
2 it went a long way in documenting what was actually
3 done on the consultations, and that would include
4 national office, which we haven't really touched on
5 here. I guess that's other people that you consult
6 with.

7 But I would strongly encourage you to leave
8 (c) in there. I think it's highly appropriate.

9 GREG SCATES: Okay. Thank you, Hal.

10 Larry Salva?

11 LAWRENCE SALVA: I agree that something
12 should be included in the standard about documentation
13 of the areas reviewed by the engagement quality
14 reviewer, but I think 19(c) is too prescriptive.
15 Especially in large and complex and multinational
16 engagements, et cetera, to say that the date of each
17 discussion, the substance of the discussion, et
18 cetera, et cetera, would become way too burdensome on
19 the process and I believe would add a lot of time
20 without significantly enhancing quality.

21 But I can appreciate that something should
22 be written similar to like what Hal just suggested. A
23 memo or something that indicates the areas that were

1 reviewed would be appropriate. But to be this
2 detailed, I think, is overly prescriptive.

3 GREG SCATES: Randy Fletchall?

4 RANDY FLETCHALL: I just want to respond to
5 Joe Carcello's observation, and I am smart enough to
6 realize with Professor Cox and a bunch of other
7 attorneys in the room, I'm not going to try to
8 articulate a difference between "known and should have
9 known" and "due professional care."

10 I think Jim Schnurr made a very valid point,
11 that due professional care is already defined for all
12 audit engagements for all roles and seems redundant.
13 Having said that, Joe, we have no objection to
14 performing the engagement quality review in accordance
15 with due professional care. So if it needs to be in
16 there to reinforce, no one is really fighting that.

17 What I think you're in objection to, and I
18 think it was laid out fairly clearly in comment
19 letters on the original exposure, was that "known or
20 should have known" is a different standard and does
21 have a legal connotation that we thought was not the
22 right objective or the right standard. And so, to see
23 the board to say, okay, we agree. We're going to

1 change it and go to due professional care, which is
2 well understood, but in the release still say, but we
3 really think it's the same thing -- it's that part of
4 it, Joe, that we're saying we don't think it is the
5 same thing.

6 And whether we have legal opinions on that
7 in our comment letters, that's the only issue, I
8 think, that's really on the table is we don't think
9 it's the same thing. And I'm not going to be -- like
10 I say, I'm too smart to take on exactly what those
11 differences are. But that's all we're really talking
12 about, not that we don't want to do the engagement
13 quality review in accordance with due professional
14 care.

15 GREG SCATES: Steve Rafferty?

16 STEVEN RAFFERTY: I'm going to switch back
17 to this 19(c) issue and sort of pile on with the
18 auditors here. I think this could be terribly
19 cumbersome, and I suspect maybe this came from the
20 issue that you couldn't tell where the concurring
21 reviewers had been in the files. But I really believe
22 19(b) probably accomplishes the objective in saying
23 the documents reviewed by the engagement quality

1 reviewer. You have to identify where they've been in
2 the file.

3 And I think requiring them to then document
4 every discussion that they have on significant issues
5 is going to be terribly cumbersome. A lot of those
6 significant issues are going to be in the form of
7 consultations that are documented in terms of what the
8 issue is, what the applicable standards are, what the
9 firm's evaluation of that is. And it's going to be
10 signed off by that concurring reviewer. So it's going
11 to be pretty obvious where they've been in the file
12 and where they've spent their time.

13 To then take and write a second memo that
14 says, "Oh, by the way, I did also discuss this with
15 the engagement team," seems a little overboard to me.

16 GREG SCATES: Thank you, Steve.

17 Vin Colman?

18 VINCENT COLMAN: Perhaps two points. Just
19 one final point in response to Joe's question by
20 Randy. I think that Paul Beswick was kind of asking
21 the question, is this a standard of performance or a
22 standard of enforcement? And I think we're getting it
23 confused, and I'd sure like to understand that because

1 I think that's where you just went, Joe. And I think
2 we've got to -- if we're going to talk about it, I
3 mean, candidly, that's kind of where you'd have to go,
4 right?

5 Because we all know what due professional
6 care is. We want to exhibit due professional care.
7 So I think there is no debate around that. But when
8 you start redefining what due professional care is, as
9 Jim said, when there's a whole standard there, and
10 then in a couple of words redefine it for enforcement
11 reasons, I think it starts getting confused.

12 These are supposed to be standards of
13 performance. Enforcement, let's decide how you handle
14 that and handle that in a different manner, at least
15 as it relates to how we would have people action a
16 standard in our firm.

17 And then moving to 19(c), again just being
18 somebody in the room who is a concurring partner on a
19 very, very large organization, when it says including
20 the date of each discussion, I would just ask that you
21 think through these words. And if you've ever kind of
22 tested it in a real-life engagement, I think that you
23 would see the cost benefit would be incredibly

1 difficult if you really understand the number of
2 interactions that go on during the course of a year if
3 you're doing -- if you're satisfying all the other
4 paragraphs of this standard.

5 GREG SCATES: Wayne Kolins?

6 WAYNE KOLINS: On that 19(c), it looks like
7 it's almost combining a couple of things. I can see
8 having that standard, and there is a standard in there
9 already for consultations during an engagement, where
10 you consult with somebody in the national accounting
11 department or whatever it happens to be, and you have
12 a significant issue that you consulted on, you
13 document that. That's fine.

14 These kinds of discussions that happen on an
15 engagement are at various levels, various gradations
16 from a very insignificant issue to very significant
17 issues, and the ultimate resolution of those
18 discussions are, hopefully, embedded in the work
19 papers. And the work papers should indicate whether
20 the concurring reviewer, engagement quality reviewer
21 reviewed those work papers.

22 So I think that that ultimate resolution was
23 already in the other parts of 19, and you don't need

1 19(c) for that reason.

2 GREG SCATES: Thank you, Wayne.

3 Sharon Fierstein?

4 SHARON FIERSTEIN: Wayne, I actually have to
5 disagree with you. I think that actually if you just
6 look at 19(a), (b), and (d), it doesn't really get the
7 whole flavor of what was done in that concurring
8 review process.

9 And while I agree that 19(c) is certainly
10 overly prescriptive and there really won't be enough
11 of a cost benefit there, it's just the benefit will
12 clearly not outweigh the cost of it. I think that
13 there does need to be some type of summary describing
14 what has gone on during that process because, frankly,
15 telling me who did it and when they did it isn't
16 really enough to tell me what was really happening in
17 that process.

18 GREG SCATES: Gaylen Hansen? Hal Schroeder?
19 Sorry.

20 HAROLD SCHROEDER: I do see a definite
21 difference between (b) and (c). You can look at whole
22 sections of an audit that have no major issues, but
23 you still thought it appropriate as a concurring

1 partner to sign off on those documents or at least
2 gain understanding.

3 And I've heard a couple of times, "Well,
4 that would be two memos in the file on an issue," and
5 I would think that there would only be the one, the
6 one that the team wrote that talks about how the
7 concurring partner was involved in that process.

8 And I'm still focusing on the word
9 "significant." I would assume that and I've heard
10 several people, "Well, they'd have to document every
11 discussion." I think we're carrying it too far. It
12 would be only those things that are significant.

13 The team would document, and then it would
14 be the concurring partner's responsibility to go and
15 sign off on those memos. Presumably, they'd be in
16 some order for it to be not a very burdensome process.

17 So I see (b) and (c) as different things,
18 and I think it's the only way to close the loop and
19 finalize what actually happened on the engagement.

20 GREG SCATES: Jim Cox?

21 JAMES COX: Yes, I sort of feel the same
22 way, Harold, that I think the point -- and it may not
23 be well expressed in 19(c). But I think the point is

1 to communicate the level of intensity of the review
2 that was carried out, the quality review. And that is
3 best communicated, I think, by identifying the areas
4 where there was some evidence of drilling down.

5 We could think about there's lots of other
6 ways of handling it, but we all live by time logs,
7 even academics, by the way. And so, we may want to
8 keep track of that and know that you've allocated a
9 significant amount of time to a particular engagement
10 and a particular inquiry. But I think the key point
11 here is "significant," and perhaps you'd like to flesh
12 that out.

13 But I think what the real issue here is so
14 that if a third party, such as the PCAOB, comes in and
15 reviews the quality of the quality reviews, they have
16 some evidence of the intensity of the review that
17 occurred. And if you don't have that, then I don't
18 think 19(a), (b), and (d) get you there.

19 GREG SCATES: Thank you, Jim.

20 Any other comments on documentation or any
21 other part? Jamie Miller?

22 JAMIE MILLER: I just want to comment on
23 this one as well. You know, I agree with the overall

1 objective of requiring documentation for the review
2 and that covering both the significant matters
3 discussed and the nature of the documents reviewed.
4 But I have to say from a cost benefit perspective, I
5 completely agree with the discussion we've had.

6 I think, as a practical matter, when you are
7 dealing with very, very large engagements where the
8 review can take hundreds, sometimes even thousands of
9 hours, I think the level of -- the prescriptive words
10 you have here may not be practicable.

11 And so, what I hear today is nobody is
12 disagreeing with the intent of what's being written.
13 It's the way it's written and the actual specific
14 requirement that's articulated in (c). So maybe that
15 could be shortened and moved to a more objectives-
16 based language?

17 GREG SCATES: Jim Cox?

18 JAMES COX: Yes, I think that that -- maybe
19 the wording suggestion is that you want to avoid sort
20 of ironclad wording, but you'd like to communicate
21 again what your objective is, and you'd like to have
22 sufficient records or documentation so that should
23 there ever be a third-party review, that one can make

1 a judgment or the records are adequate to feel
2 comfortable with the level of intensity that was
3 appropriate given the challenges of the review.

4 GREG SCATES: Any more comments on
5 documentation or any other aspect of the engagement
6 quality review that we've discussed today?

7 Gary?

8 GARY KABURECK: I have one on a subject we
9 haven't discussed if you're moving to a general
10 discussion.

11 And actually up on question one, where
12 you're talking about types of engagements, you've got
13 an audit. You've got the inner reviews. And as a
14 general statement, I would agree those are the ones
15 you need to do, and a lot of other agreed-upon
16 procedures or long-form report for some due diligence,
17 those aren't necessary.

18 But did you consider requiring an engagement
19 quality review for SAS 70 reports? I'm thinking
20 particularly SAS 70 Type II, thinking for our own SOX
21 procedures. I mean there is a lot of stuff is
22 outsourced to vendors and information providers and so
23 on. And that's sort of where the world is going these

1 days, more and more outsourcing, more and more
2 offshoring to specialists.

3 So I've found over the five years we've been
4 doing the 404 work, we actually have more SAS 70
5 reports now than we did in year one because just the
6 normal evolution of business. The question is, should
7 you require an engagement quality review for a SAS 70
8 report that you're issuing? Did you consider it?

9 My instincts tell me it probably is a good
10 thing. I don't know if it's a great thing, and I
11 don't even know if I'd hold up finalizing this and
12 deal with it separately. But was it considered and
13 listen for reaction from anybody else.

14 GREG SCATES: We certainly would appreciate
15 your comments, Gary, and any others of anything, any
16 type of report that we should consider that should be
17 subject to an engagement quality review, and we would
18 like to have that in a comment letter.

19 And if there's anything else, Gary, or
20 anyone else, any other item that we should consider
21 including, please let us know. Let us know now or in
22 a comment letter, let us know if there's anything else
23 we should consider.

1 Yes, Gaylen Hansen?

2 GAYLEN HANSEN: I happen to agree that the
3 SAS 70, and you can't really rely on a Type I, but a
4 Type II. We're seeing more and more of those in
5 practice, and the reliance on those are significantly
6 increasing in quantity and volume. So reliance on
7 information service providers, I think, is going to be
8 part of where this profession is going, and I would
9 look forward rather than go through this standard and
10 leave it out. But maybe consider pulling that into
11 the standard.

12 GREG SCATES: Thank you, Gaylen.

13 Any other comments?

14 [No Response.]

15 GREG SCATES: Okay. Well, I thank you for
16 your input, and I want to remind you that the comment
17 period ends on April 20th. And we would -- I
18 encourage you to write comment letters, anything you
19 mentioned today or anything you want to comment on in
20 the release. I encourage you to get those letters
21 into us.

22 As you can see from this reproposal the
23 impact that those comment letters had on the staff and

1 the board, and we certainly appreciate your input.

2 I now turn the meeting over to Jennifer

3 Rand.

4 JENNIFER RAND: Thanks, Greg. And thanks

5 again for your input in connection with that

6 discussion.



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AUDITING STANDARD No. 7 –)	PCAOB Release No. 2009-004
)	July 28, 2009
ENGAGEMENT QUALITY REVIEW)	
)	PCAOB Rulemaking
AND CONFORMING AMENDMENT TO THE)	Docket Matter No. 025
BOARD'S INTERIM QUALITY CONTROL)	
STANDARDS)	
)	
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Summary: After public comment, the Public Company Accounting Oversight Board (the "Board" or "PCAOB") is adopting an auditing standard, *Engagement Quality Review*, that will be applicable to all registered firms and will supersede the Board's interim concurring partner review requirement, and a conforming amendment to the Board's interim quality control standards.

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I. Introduction

Section 103 of the Sarbanes-Oxley Act (the "Act") directs the Board, among other things, to set standards for public company audits, including a requirement for each registered public accounting firm to "provide a concurring or second partner review and approval of [each] audit report (and other related information), and concurring approval in its issuance" A well-performed engagement quality review ("EQR") can serve as an important safeguard against erroneous or insufficiently supported audit opinions and, accordingly, can contribute to audit quality. In February 2008, the Board proposed to replace its interim requirement with a new EQR standard.^{1/} The Board's

^{1/} PCAOB Release No. 2008-002, Proposed Auditing Standard – *Engagement Quality Review and Conforming Amendment to the Board's Interim Quality Control Standards* (February 26, 2008) (the "original proposal").



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original proposal was developed in response, among other things, to feedback from some members of its Standing Advisory Group ("SAG") that the existing interim requirements^{2/} (the "existing requirements") do not provide for a sufficiently thorough review to give investors assurance on the quality of engagements. The proposal was intended to enhance the quality of the EQR by strengthening the existing requirements.

Commenters recommended significant modifications to the original proposal, and, in response, the Board made changes designed to better tailor the standard to its purposes.^{3/} Because of the extent of those changes, the Board again sought public comment, this time on the standard as revised. The Board has considered those comments, as well as the input of the SAG, and the final standard ("AS No. 7" or the "EQR standard") has benefitted from the additional public input.^{4/}

The EQR standard the Board is adopting provides for a rigorous review that will serve as a meaningful check on the work performed by the engagement team. AS No. 7 should increase the likelihood that a registered public accounting firm will catch any significant engagement deficiencies before it issues its audit report. As a result, the Board recognizes that more work may be necessary under the EQR standard than was performed in some concurring reviews under the existing requirements.

At the same time, the Board has been sensitive to commenters' concerns and agrees that the EQR should not become, in effect, a second audit. Instead, the EQR should be – and, as described in AS No. 7, is – a review of work already performed by the engagement team. The EQR standard requires the engagement quality reviewer (or the "reviewer") to evaluate the significant judgments made and related conclusions

^{2/} The Securities and Exchange Commission Practice Section ("SECPS") of the American Institute of Certified Public Accountants ("AICPA") Requirements of Membership Sections 1000.08(f); 1000.39, Appendix E.

^{3/} Comments on the original proposal and the Board's responses are described in PCAOB Release No. 2009-001, Proposed Auditing Standard – *Engagement Quality Review* (March 4, 2009) (the "reproposing release").

^{4/} The Board received 38 comments on the original proposal and 30 comments on the reproposal. The SAG discussed the repropounded standard on April 2, 2009. A transcript of that discussion is available on the Board's website at http://www.pcaobus.org/Rules/Docket_025/index.aspx. The SAG also discussed EQR on June 22, 2004 and October 5, 2005. Archived webcasts are available on the Board's website at http://www.pcaobus.org/News_and_Events/Webcasts.aspx.



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reached by the engagement team in forming the overall conclusion on the engagement and in preparing the engagement report, and requires certain procedures designed to focus the reviewer on those judgments and conclusions.

The procedures required of the reviewer by AS No. 7 are different in nature from the procedures required of the engagement team. Unlike the engagement team, a reviewer does not perform substantive procedures or obtain sufficient evidence to support an opinion on the financial statements or internal control over financial reporting. If more audit work is necessary before the reviewer may provide concurring approval of issuance, the engagement team – not the reviewer – is responsible under PCAOB standards for performing the work. In contrast, the reviewer fulfills his or her responsibility to perform an effective review of the engagement under the EQR standard by holding discussions with the engagement team, reviewing documentation, and determining whether he or she can provide concurring approval of issuance.

II. Overview of Auditing Standard No. 7

Overall, commenters preferred the repropoed standard to the original proposal, though some continued to believe that certain provisions were unclear and suggested certain changes to the standard. After considering commenters' feedback, the Board has made several modifications to the EQR standard to provide additional clarity. This section describes the comments received, the Board's response, and changes made in AS No. 7.^{5/}

A. **Applicability of the EQR Requirement**

Paragraph 1 of the repropoed standard required an EQR for audit engagements and reviews of interim financial information ("interim reviews"), but not for other engagements performed according to the standards of the PCAOB. For the most part, commenters believed that this provision was appropriate.^{6/} One commenter, however, suggested including the EQR requirements for interim reviews in AU section ("sec.")

^{5/} The Board received some comments related to its standard-setting process in general. The Board continuously endeavors to improve its processes, including its standard-setting process, and is considering these comments as it does so.

^{6/} One commenter did not believe that an EQR should be required for interim reviews because of concerns about the scope of the EQR for interim reviews. The section entitled *Specifically Required Procedures in the EQR of an Interim Review* of this release discusses the EQR requirements for interim reviews.



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722, *Interim Financial Information*, instead of including them as part of the EQR standard to "make it clear that the scope of the procedures performed remain under the umbrella of the objective of a review of interim financial information (which is much different than the scope and objective of an audit)." Because the requirements for the EQR of interim reviews in AS No. 7 are closely related to and described by reference to the requirements for the EQR of an audit, the Board believes it is more appropriate to locate both sets of requirements in the same standard. Accordingly, the Board is adopting the provisions regarding applicability of the EQR standard as repropoed.

B. Statement of Objective

The repropoed standard included a statement of objective intended to focus reviewers on the overall purpose of the standard as they carry out the more specific EQR requirements. As repropoed, the objective of the engagement quality reviewer was "to perform an evaluation of the significant judgments made by the engagement team and the conclusions reached in forming the overall conclusion on the engagement and in preparing the engagement report, if a report is to be issued, in order to determine whether to provide concurring approval of issuance."

Most commenters agreed that the EQR standard should include a statement of objective. While some believed the objective was appropriate as repropoed, several suggested substituting the phrase "related conclusions reached" for "the conclusions reached" to indicate that the reviewer is required to evaluate conclusions relating to significant judgments, rather than all conclusions. In addition, some commenters suggested making the objective less vague, while others wanted the Board to broaden it or make it less procedural.

After considering these comments, the Board has, as suggested by commenters, revised the objective so that it refers to "significant judgments made by the engagement team^{7/} and the *related* conclusions reached" (emphasis added). This change should help reviewers maintain their focus on areas of the engagement that are most likely to contain a significant engagement deficiency. With this revision, the Board

^{7/} Because the engagement partner has final responsibility for the engagement, he or she has final responsibility for the significant judgments made during the engagement, notwithstanding any involvement in or responsibility for those judgments by firm personnel outside of the engagement team, such as members of the firm's national office. Accordingly the "significant judgments made by the engagement team" include all of the significant judgments made during the engagement.



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believes the statement of objective establishes, at the appropriate level of detail, a framework for the performance of the EQR that is consistent with the specific requirements in AS No. 7. Corresponding changes have been made in paragraphs 9 and 14, which describe the scope of the EQR for audits and interim reviews, respectively. The reviewer achieves his or her objective by complying with the specific requirements of the standard.

C. Qualifications of the Engagement Quality Reviewer

In order to provide for a high-quality EQR, the repropoed standard described the qualifications that any reviewer would be required to meet. These provisions were designed to provide assurance that the reviewer could effectively perform an EQR of the particular engagement under review. At the same time, the provisions recognized that smaller firms may have few partners – and, in the case of sole practitioners, no additional partners – available in-house to perform the EQR.

Accordingly, the repropoed standard required an engagement quality reviewer from within the firm issuing the engagement report to be a partner or another individual in an equivalent position, but also allowed a qualified individual from outside the firm to perform the EQR. In either event, the repropoed standard required the reviewer to be an associated person^{8/} of a registered public accounting firm.^{9/} The repropoed standard

^{8/} For clarity, in paragraph 3 of AS No. 7, the Board added a reference to Rule1001(p)(i), which defines the term "associated person of a registered public accounting firm." A person not already associated with a registered firm can enter into a relationship with the firm issuing the report such that the person would become associated with that firm by performing the review. Specifically, a person not already associated with a firm would become associated with the firm issuing the report if *he or she* (rather than, or in addition to, his or her firm or other employer): (1) receives compensation from the firm issuing the report for performing the review or (2) performs the review as agent for the firm issuing the report. For example, if the firm issuing the report contracts directly with an employee of an unregistered accounting firm to perform the engagement quality review, that person would become associated with the firm issuing the report by virtue of that independent contractor relationship.

^{9/} A registered public accounting firm has an obligation to secure and enforce consents to cooperate with the Board from each associated person of the firm, see Section 102(b)(3) of the Act, including those who become associated with the firm by performing the review. The Board also may directly sanction any such person who



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also included a general competence requirement and requirements related to the reviewer's independence, integrity, and objectivity.

In-House Reviewer: Partner or an Individual in an Equivalent Position

The requirement in the reposed standard for a reviewer from within the firm to be a partner or an individual in an equivalent position was intended to address concerns expressed by some commenters on the original proposal about the authority of the engagement quality reviewer relative to that of the engagement partner. Because the EQR is intended to be an objective second look at work performed by the engagement team, the reviewer should be able to withstand pressure from the engagement partner or other firm personnel, such as members of the firm's national office. As described in the reposing release, the Board believed that concerns about authority will most often arise when the reviewer and the engagement partner work at the same firm. The Board also believed that a standard based on perceptions of relative authority within a firm would not be sufficiently clear to be workable. Accordingly, the Board attempted to address these concerns with a requirement that an in-house reviewer – but not one from outside the firm – be a partner or person in an equivalent position.

While some commenters supported the reposed requirement, others disagreed with it, generally because, in their view, being a partner or person in an equivalent position would not necessarily ensure that the reviewer possesses the qualities required to perform the EQR. These commenters noted that partners as well as non-partners may be subject to internal pressure within the firm to provide concurring approval of issuance. In addition, in one commenter's view, it would be burdensome for one-partner firms to hire an outside reviewer to comply with this requirement. Finally, some commenters also asked the Board to define the term "equivalent position."

While both partners and non-partners may experience pressure within the firm to provide concurring approval of issuance, the Board continues to believe that the reposed requirement is the most appropriate way to address this issue. Partnership is not a perfect proxy for authority, but a partner is more likely to possess sufficient authority to conduct the EQR than a non-partner. The Board continues to believe that a requirement based on perceptions of authority would not be workable. Accordingly, the

fails to cooperate in an investigation or inspection. See Section 105(b)(3) of the Act and PCAOB Rules 5110 and 4006.



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Board is adopting this requirement substantially as repropoed.^{10/} At a firm that is not organized as a partnership, "an individual in an equivalent position" is someone with the degree of authority and responsibility of a partner in a firm that is organized as a partnership.

Qualified Reviewer from Outside the Firm

As noted above, the repropoed standard also allowed a qualified reviewer from outside the firm to conduct the review. In the repropoing release, the Board expressed the view that allowing a sufficiently qualified professor or other individual not employed by an accounting firm to perform the EQR should not negatively affect audit quality and may mitigate the compliance burden on sole practitioners and smaller firms. The Board sought comment on whether a qualified accountant who is not employed by an accounting firm should be allowed to conduct the EQR.^{11/}

The majority of commenters on this topic did not oppose the repropoed provision. Some commenters, however, cautioned that reviewers from outside an accounting firm may not necessarily have the required technical expertise or recent audit experience. One commenter believed that allowing the use of such outside reviewers could "hamper the existing independence rules,"^{12/} increase costs, and limit the potential growth of partners.

After considering these comments, the Board continues to believe that the EQR standard can – and should – allow firms the proposed flexibility in choosing a reviewer, provided that reviewer meets the competence and other qualification requirements.

^{10/} One commenter suggested that the phrasing of the repropoed standard did not establish a requirement for the in-house reviewer to be a partner because it stated that the reviewer "may be" a partner, a person in an equivalent position, or an individual outside the firm. While the use of "may" in that context imposed a requirement, to avoid any confusion on this point the Board has rephrased the requirement in paragraph 3 of AS No. 7 to use the word "must."

^{11/} As noted in the repropoing release, under the existing requirement a firm may seek a waiver to engage an outside experienced individual to perform the EQR. Because AS No. 7 allows a firm to use an outside reviewer, such a waiver is not necessary under AS No. 7.

^{12/} The comment did not explain how the independence rules would be hampered.



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According to these requirements, as discussed below, any reviewer would have to have the level of knowledge and competence related to accounting, auditing, and financial reporting required to serve as the person who has overall responsibility for the engagement under review. Accordingly, while some persons from outside a firm might not have the required qualifications, those who do can effectively perform the EQR.^{13/}

The Board also does not agree that allowing the use of a reviewer from outside the firm issuing the report would negatively affect the application or enforcement of the independence rules. As the Board noted in the reproposing release, it will continue to consider anyone who performs the EQR to be an "audit partner" and a member of the "audit engagement team" for purposes of independence requirements.^{14/} In addition, because AS No. 7 would not require a firm to use an outside reviewer, allowing a firm to do so should not increase costs or limit the potential growth of partners. Any firm that is concerned that invoking the flexibility provided by the EQR standard would raise its costs or impede the development of its partners could, simply, decline to do so and use a reviewer from within the firm if one is available.

When considering an outside individual for the role of the engagement quality reviewer, the firm will likely need to make additional inquiries to obtain necessary information about the individual's qualifications. For example, while information about independence of the firm's partners is typically collected and evaluated as part of the periodic independence review, information about the independence of an outside reviewer will likely need to be requested and evaluated as part of the reviewer selection process. Firms also likely know more about the competence of their own partners than of an outside reviewer.

General Competence Requirement

As noted above, the reproposed standard, like the original proposal, included a requirement for the reviewer to "possess the level of knowledge and competence related to accounting, auditing, and financial reporting required to serve as the person who has overall responsibility for the same type of engagement." This provision was intended to set a minimum requirement for those who would perform the EQR. In response to comments on the original proposal, the reproposing release explained that

^{13/} Similarly, a reviewer does not meet all of the qualification requirements in AS No. 7 by virtue of his or her status as a partner or employee of an accounting firm.

^{14/} See Rule 2-01(f) of Regulation S-X, 17 C.F.R. § 210.2-01(f), for the definitions of "audit partner" and "audit engagement team."



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this provision, by its terms, did not require the engagement quality reviewer's knowledge and competence to match those of the engagement partner, or for the reviewer to be a "clone" of the engagement partner.^{15/}

Some commenters reiterated their concerns that the engagement quality reviewer's skills would be expected to match those of the engagement partner, and that such a requirement could cause resource constraints for smaller firms. Other commenters suggested modifying the general competence provision by stating that the reviewer's competence should be established based on the facts and circumstances of the engagement, or describing the required qualifications from the reviewer's perspective, rather than by comparing them to the qualifications of the engagement partner. Finally, some commenters suggested including in the EQR standard a statement that the reviewer may obtain the required level of knowledge and competence through utilizing assistants.

The Board continues to believe that if a minimum level of knowledge and competence in accounting, auditing, and financial reporting is required to conduct an audit, it is similarly necessary to effectively review that audit.^{16/} The reviewer is not required to possess other competencies, e.g., those related to communication or management skills, that the engagement partner may have.

Accordingly, the Board is adopting the general competence provision substantially as proposed. The Board is, however, modifying the requirement to clarify further that the determination of what constitutes the appropriate level of knowledge and competence should be based on the circumstances of the engagement, including the size and complexity of the business under audit or under interim review.^{17/} In AS No. 7,

^{15/} Specifically, the reproposing release noted:

The general competence provision merely sets a minimum requirement for those who would perform the EQR, but it does not require the reviewer's competence to match that of the engagement partner. In many cases, both individuals' competence will exceed the minimum level prescribed, but there is no requirement that they do so in tandem, or even at all.

^{16/} While a reviewer may use assistants in performing the EQR, the reviewer's own skills should meet the requirements of AS No. 7.

^{17/} Footnote 18 on page 9 of the original release stated, "The determination of what constitutes the appropriate level of knowledge and competence should be based



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the Board replaced the phrase "the same type of engagement" with "the engagement." The new phrasing focuses the reviewer on the particular engagement under review, rather than that "type" of engagement.^{18/} Firms that do not have partners that meet this general competence requirement available to perform the EQR may engage an outside reviewer to perform an EQR.

Independence, Integrity, and Objectivity

Like the original proposal, the repropoed standard required the reviewer to be independent of the company, perform the review with integrity, and maintain objectivity. Comments on the repropoal focused on two provisions regarding objectivity – the prohibition against the reviewer supervising the engagement team and the two-year "cooling-off" period before the engagement partner could perform the EQR.

Supervision of the Engagement Team

The repropoed standard provided that to maintain objectivity the engagement quality reviewer should not, among other things, "supervise the engagement team with respect to the engagement subject to the engagement quality review." The phrase "subject to the engagement quality review" was intended to clarify that partners with leadership responsibilities in a firm, region, service, or industry practice are not, solely because of those responsibilities, precluded from reviewing any engagement performed by their subordinates in the firm. Some commenters believed that the phrase "subject to the engagement quality review" was not sufficient to clarify this point.

on the circumstances of the engagement, including the size or complexity of the business."

^{18/} In addition, to simplify the text of AS No. 7, the Board replaced the phrase "person with overall responsibility for the engagement" with the term "engagement partner." Footnote 3 of AS No. 7 explains that the term "engagement partner" has the same meaning as the phrases the "auditor with final responsibility for the audit," as described in AU sec. 311, *Planning and Supervision*, and the "practitioner-in-charge of an engagement," as described in PCAOB interim quality control standard QC sec. 40, *The Personnel Management Element of a Firm's System of Quality Control-Competencies Required by a Practitioner-in-Charge of an Attest Engagement*. Because all of these terms refer to the same person, this change does not alter the meaning of the EQR standard.



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After considering these comments, the Board has decided that the express prohibition against "supervis[ing] the engagement team with respect to the engagement subject to the engagement quality review" is not necessary to effectuate the Board's intent. The remaining two criteria for maintaining objectivity in paragraph 7 of AS No. 7 – not making decisions on behalf of the engagement team and not assuming any responsibilities of the engagement team – are sufficient to preclude those involved in the engagement from serving as the engagement quality reviewer.^{19/} For example, partners (including the engagement partner and other partners on larger engagements), managers, and others who supervise engagement personnel on the audit under review would not qualify under the remaining criteria because they have assumed responsibilities of the engagement team. At the same time, removing the phrase "supervise the engagement team" from AS No. 7 should further clarify that those in leadership positions in the firm who did not make decisions for or assume responsibilities of the engagement team may perform the EQR.

The Two-Year "Cooling-Off" Period

The repropoed standard included a provision prohibiting an engagement partner from serving as the engagement quality reviewer for at least two years following his or her last year as the engagement partner.^{20/} The Board included the "cooling-off" period because it believed that it would be harder for an engagement partner who has had overall responsibility for the audit for at least a year to perform the review with the

^{19/} AS No. 7 does not prohibit the engagement team from consulting with the reviewer, as long as the reviewer maintains his or her objectivity in accordance with paragraph 7. As noted in the repropoing release, such consultations may contribute to audit quality. In addition, one commenter asked the Board to clarify whether a reviewer may consult with the same personnel who previously consulted with the engagement team. The EQR standard does not prohibit the reviewer from holding discussions with such personnel. The reviewer may not, however, use personnel who previously consulted with the engagement team as assistants in performing the review unless they meet the objectivity and other qualification requirements of AS No. 7. To emphasize the requirement that assistants maintain objectivity, the Board added to paragraph 7 of AS No. 7 the phrase "and others who assist the reviewer."

^{20/} SEC independence rules allow engagement partners and concurring partners to serve for five consecutive years, after which they may not serve in either role for another period of five years. Within a five-year period, SEC independence rules do not impose a "cooling-off" period before the engagement partner can serve as the concurring partner. See Rule 2 - 01(c)(6)(i)(A) of Regulation S-X.



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necessary level of objectivity. While a number of commenters expressed general support for a two-year "cooling-off" period, some believed that it could impose an undue hardship on smaller firms, and suggested a shorter "cooling-off" period.

After considering these comments, the Board continues to believe that a "cooling-off" period will be beneficial to audit quality and that a two-year period appropriately safeguards objectivity without imposing unnecessary hardship on most firms. At the same time, the Board recognizes that compliance with this requirement could be difficult for smaller firms with fewer personnel. In its independence rules, the Securities and Exchange Commission ("SEC") exempted certain smaller firms from the audit partner rotation requirements. Specifically, Rule 2-01(c)(6)(ii) of Regulation S-X provides an exemption for firms with fewer than five issuer audit clients and fewer than ten partners, provided the Board "conducts a review at least once every three years of each of the audit client engagements that would result in a lack of auditor independence under" the SEC partner rotation requirements. The Board believes that this exemption – including the provision regarding Board inspections – also describes an appropriate exemption from the "cooling-off" requirement in the EQR standard. Accordingly, firms that qualify for the exemption from the SEC partner rotation requirements will also be exempt from the "cooling-off" period under AS No. 7.

D. EQR Process

The Board's goal in proposing an EQR standard was to strengthen the existing requirements for concurring reviews in order to promote a more meaningful review of the work performed by the engagement team. Accordingly, the original proposal described certain procedures that the reviewer was required to perform that were more specific than those in the existing requirements. In response to comments received on the original proposal, the Board clarified some of the specifically required procedures and included, in a separate section in the repropoed standard, tailored requirements for an EQR of an interim review.

In general, commenters believed that the repropoed standard described the requirements of the EQR more clearly than the original proposal. However, a number of commenters suggested additional modifications that, in their view, would further clarify the Board's intent and ensure consistency of the requirements with the statement of objective. As described below, after considering these comments, the Board has modified certain of these requirements.



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Terminology Used to Describe the Required Procedures

Several commenters noted that the specifically required procedures in paragraphs 9, 10, 14, and 15 of the repropoed standard were described using different, but in some cases similar, terms such as "determine," "evaluate," "identify," "read," and "review," which some commenters found confusing. In one commenter's view, the terms "determine," "identify," and "evaluate" may require the reviewer to perform procedures that are similar in scope to the procedures performed by the engagement partner. The commenters asked the Board to clarify the terminology in these sections of the EQR standard.

While the Board does not believe that this terminology required the reviewer to perform procedures that are appropriately performed by the engagement partner, it does agree that the terminology should not be confusing. Accordingly, the Board reduced the number of terms used in AS No. 7, so that the required procedures in paragraphs 9, 10, 14, and 15 are described using two terms, "evaluate" and "review" – with one exception. Because AU sec. 550, *Other Information in Documents Containing Audited Financial Statements*, requires the auditor to *read* other information in documents containing the financial statements to be filed with the SEC, paragraphs 10.g and 15.e of AS No. 7, like in the original and repropoed standards, also require the reviewer to *read* such other information and evaluate whether the engagement team has taken appropriate action with respect to any material inconsistencies with the financial statements or interim financial information, respectively, or material misstatements of fact of which the engagement quality reviewer is aware.

Review of Documentation

A number of commenters viewed the statement in paragraphs 9 and 14 of the repropoed standard that "the reviewer should perform the procedures . . . by reviewing documentation" as too open-ended.^{21/} Commenters were concerned that this provision could be interpreted to require the review of all of the engagement documentation.

The Board did not intend to require – and the repropoed provision did not require – the reviewer to review all of the engagement documentation. Nevertheless, to clarify this point, the Board has added the phrase "to the extent necessary to satisfy the

^{21/} That statement was intended, along with other changes in the repropoed standard, to clarify that the EQR is a review of the engagement team's work rather than a second audit. See page 17 of the repropoing release.



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requirements" of paragraphs 10 and 11, in an EQR of an audit, and 15 and 16, in an EQR of an interim review. As a practical matter, the reviewer cannot comply with the requirements of the EQR standard without holding discussions with the engagement partner and reviewing documentation. AS No. 7 requires the reviewer to hold sufficient discussions with the engagement partner and other members of the engagement team and review sufficient documentation to perform the required procedures with due professional care. What is sufficient will necessarily depend on the facts and circumstances of the particular engagement under review. Auditors often document their significant judgments and conclusions in various summary documents, which could serve as a starting point for the reviewer's evaluation of the engagement team's work.

Paragraph 11 of the repropoed standard required the reviewer, in an EQR of an audit, to evaluate whether the engagement documentation that he or she reviewed when performing the procedures required by paragraph 10 indicates that the engagement team responded appropriately to significant risks and supports the conclusions reached by the engagement team with respect to the matters reviewed. One commenter suggested adding a requirement to paragraph 11 to evaluate engagement documentation for compliance with the requirements of Auditing Standard No. 3, *Audit Documentation* ("AS No. 3"). The Board originally proposed such a requirement but, in response to comments, did not include it in the repropoed standard.^{22/} The Board continues to believe that the documentation review requirements of paragraph 11 of the repropoed standard are appropriate and is adopting them as repropoed.

In an EQR of an interim review, paragraph 16 of the repropoed standard required the reviewer to evaluate whether the engagement documentation that he or she reviewed "[i]ndicates that the engagement team responded appropriately to significant risks," and "[s]upports the conclusions reached by the engagement team with respect to the matters reviewed." Some commenters noted that the auditor is not required to identify significant risks in a review of interim financial information and suggested not including a corresponding requirement in the EQR standard. The Board agrees and has not included this requirement in AS No. 7.

^{22/} Commenters suggested that such a requirement would duplicate the documentation review performed by the engagement partner.



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Specifically Required Procedures in the EQR of an Audit

Like the original proposal, the repropoed standard required certain procedures designed to give the reviewer the necessary information to evaluate the engagement team's significant judgments and conclusions. In response to comments on the original proposal, the Board made changes to these provisions in the repropoed standard that were intended to clarify that the reviewer performs the EQR by reviewing the engagement team's work, rather than by auditing the company himself or herself. Some commenters suggested that the specifically required procedures in the repropoed standard needed additional clarification.

In the view of several commenters, the repropoed standard did not clearly articulate the requirement for the reviewer to focus on the significant judgments made and the related conclusions reached by the engagement team. These commenters believed that the repropoed standard might be interpreted as requiring the review of all of the engagement team's judgments and conclusions. In response, AS No. 7 refers to "significant judgments" instead of "judgments" in describing certain of the required procedures.

The Board also clarified the wording of paragraph 10.b of the repropoed standard, which required the reviewer to "evaluate the risk assessments and audit responses" Some commenters expressed concern that this formulation required a review of audit responses for all areas of the audit. In response, AS No. 7 more specifically requires the reviewer to evaluate the engagement team's audit responses to significant risks identified by the engagement team and other significant risks identified by the engagement quality reviewer through performance of the procedures required by the EQR standard.^{23/} This change should help focus reviewers on areas of the audit that are more likely to contain a significant engagement deficiency.

^{23/} The term "significant risk" is defined in the Board's recently proposed auditing standard on identifying and assessing risks of material misstatement to mean a "risk of material misstatement that is important enough to require special audit consideration." PCAOB Release No. 2008-006, *Proposed Auditing Standards Related to the Auditor's Assessment of and Response to Risk and Conforming Amendments to PCAOB Standards* (October 21, 2008). The Board intends that definition to apply to the EQR standard as well. The Board included this definition in a note to paragraph 10.b of AS No. 7. If, at the conclusion of the above mentioned rulemaking, the Board adopts a



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Some commenters also expressed concern about the requirements in paragraphs 10.e and 10.f of the repropoed standard to determine whether appropriate matters have been communicated to the audit committee, management, and others; and to determine whether appropriate consultations have taken place on difficult or contentious matters. According to these commenters, a requirement to determine whether all of the communications or consultations have taken place rather than to evaluate the engagement team's communications and consultations was inconsistent with the objective of the EQR. In response, the Board replaced the phrase "determine if" with "based on the procedures required by this standard, evaluate whether." This change should tailor the specific requirements more closely to the overall objective. The Board also placed these paragraphs after the other required procedures in paragraph 10 to emphasize that the reviewer performs the evaluation required by these paragraphs based on the information obtained through the other procedures required by the EQR standard, and made a corresponding change in paragraph 15 for the EQR of an interim review.

Specifically Required Procedures in the EQR of an Interim Review

In response to comments on the original proposal, the Board included in the repropoed standard separate requirements for reviewing audits and interim reviews. The EQR requirements for interim reviews were based on the requirements for an EQR of an audit but were tailored to the different procedures performed in an interim review. A number of commenters were supportive of including separate requirements for the EQR of interim reviews in the repropoed standard. Some commenters, as discussed below, suggested modifications to those requirements.

Paragraph 15.a of the repropoed standard required the evaluation of engagement planning, including the consideration of the firm's recent engagement experience with the company and risks identified in connection with the firm's client acceptance and retention process; the company's business, recent significant activities, and related financial reporting issues and risks; and the nature of identified risks of material misstatement due to fraud. In one commenter's view, that paragraph might suggest that an interim review should include the same type of risk assessment as an audit. After considering this comment, the Board disagrees. Paragraph 15.a does not impose a requirement on the engagement team to identify risks as part of an interim review. Rather, it requires the reviewer to evaluate the engagement team's

definition of significant risk that is different from that proposed, the Board will make a conforming change to the EQR standard.



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consideration of risks that have already been identified, e.g., during the preceding year's audit.

Additionally, three commenters recommended not requiring the EQR of an interim review to include an evaluation of judgments made about the severity and disposition of identified control deficiencies. In one commenter's view, such an evaluation would be inconsistent with the scope of an interim review. AU sec. 722.07, provides that the auditor:

should perform limited procedures quarterly to provide a basis for determining whether he or she has become aware of any material modifications that, in the auditor's judgment, should be made to the disclosures about changes in internal control over financial reporting in order for the certifications to be accurate and to comply with the requirements of Section 302 of the Act.

In response, the Board modified the requirement in paragraph 15.b in AS No. 7 to be more consistent with the requirements of AU sec. 722. Accordingly, AS No. 7 requires the reviewer, among other things, to evaluate significant judgments made about any material modifications that should be made to the disclosures about changes in internal control over financial reporting.

Paragraph 15.c of the reproposed standard required the reviewer, in the EQR of an interim review, to "[r]ead the interim financial information for all periods presented and for the immediately preceding interim period, management's disclosure for the period under review, if any, about changes in internal control over financial reporting, and the related engagement report, if a report is to be filed with the SEC." Some commenters suggested that the reviewer should be required to read the engagement report even when the issuer is not required to include the report in an SEC filing. The Board agrees and, accordingly, changed "to be filed with the SEC" to "to be issued."^{24/}

^{24/} Additionally, one commenter recommended not requiring the reviewer to read interim financial information "for the immediately preceding interim period" because it was not clear, to this commenter, what one would review when performing the EQR for the first quarter. AU sec. 722.16 requires the accountant to apply analytical procedures to the interim financial information, which should include, among other things, comparing the quarterly interim financial information with comparable information for the immediately preceding interim period (i.e., the fourth quarter of the prior year, in a first quarter interim review). Because the Board believes the reproposed requirement



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E. Concurring Approval of Issuance

For an EQR of an audit, paragraph 12 of the repropoed standard provided that the reviewer "may provide concurring approval of issuance only if, after performing with due professional care the review required by this standard, he or she is not aware of a significant engagement deficiency." A note to the same paragraph describes a "significant engagement deficiency" as any of the four conditions described in the original proposal.^{25/} The repropoed requirements for providing concurring approval of issuance in an EQR of an interim review were the same, except that the first of these four conditions was modified in light of the differences between an interim review and an audit. Specifically, in an EQR of an interim review, the first condition was "the engagement team failed to perform interim review procedures necessary in the circumstances of the engagement" rather than "the engagement team failed to obtain sufficient appropriate evidence in accordance with the standards of the PCAOB."

Commenters generally believed that the concurring approval of issuance provision was appropriately described, though one recommended excluding the reference to "due professional care" from the EQR standard because AU sec. 230, *Due Professional Care in the Performance of Work*, already imposes an overall requirement on auditors to exercise due professional care. Many commenters, however, were critical of the repropoing release's description of the repropoed requirement. A significant number of commenters objected to, or stated that they disagreed with, the statement in the repropoing release that the requirement to exercise due professional care imposes on the engagement quality reviewer essentially the same requirement as the "knows, or should know based on the requirements of this standard" formulation that was originally proposed. Some suggested that the Board is redefining the meaning of due professional care. One commenter stated that "[a] standard of 'knows, or should know' is akin to a strict liability requirement for engagement deficiencies," while another commenter suggested that the Board "clarify that in this context, 'due professional care' is not a negligence standard."

is appropriately within the scope of an EQR for an interim review, it has retained it in AS No. 7.

^{25/} As included in the repropoed standard, these conditions were: (1) the engagement team failed to obtain sufficient appropriate evidence in accordance with the standards of the PCAOB; (2) the engagement team reached an inappropriate overall conclusion on the subject matter of the engagement; (3) the engagement report is not appropriate in the circumstances; or (4) the firm is not independent of its client.



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After considering the comments, the Board is adopting the concurring approval of issuance requirement as repropoed. While auditors are already required to exercise due professional care in discharging their responsibilities, comments, as noted above and in the repropoing release, have reflected some confusion about the applicable standard of care in an EQR. Accordingly, reference to due professional care in the requirement is appropriate.

The Board is not redefining due professional care in the context of the EQR standard. As the Board noted in the repropoing release, AU sec. 230 describes due professional care as "reasonable care and diligence" and makes clear that an auditor who acts negligently, i.e., without "reasonable care and diligence," breaches the duty to exercise due professional care.^{26/} Due professional care, as described in AU sec. 230, imposes neither a strict liability nor an actual knowledge standard. The Board intends the term to mean "reasonable care and diligence," as described in AU sec. 230.

The application of a negligence standard to the concurring approval of issuance provision means, as noted in the repropoing release, that "a reviewer cannot evade responsibility because, as a result of an inadequate review, he or she did not discover a problem that a reasonably careful and diligent review would have revealed."^{27/} For that reason, the provision requires the reviewer to perform the required review with due professional care as a prerequisite to providing concurring approval of issuance. A qualified reviewer who has done so will, necessarily, have discovered any significant engagement deficiencies that could reasonably have been discovered under the circumstances. Accordingly, under AS No. 7, such a reviewer may provide concurring approval of issuance if "he or she is not aware of a significant engagement deficiency." Because a reviewer who has not performed the required review with due professional care might not have discovered any significant engagement deficiencies that could reasonably have been discovered under the circumstances – i.e., those the reviewer

^{26/} See AU sec. 230.03.

^{27/} Of course, to impose the more severe sanctions authorized under the Act, such as a permanent bar or permanent revocation of registration, the Board must establish "(A) intentional or knowing conduct, including reckless conduct, that results in violation of the applicable statutory, regulatory, or professional standard; or (B) repeated instances of negligent conduct, each resulting in a violation of the applicable statutory, regulatory, or professional standard." Section 105(c)(5) of the Act; see also Rules on Investigations and Adjudications, PCAOB Release No. 2003-015, Appendix 2 at A2-76 (September 29, 2003) (discussing Section 105(c)(5)).



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reasonably should know about – such a reviewer may not, consistent with the standard, provide concurring approval of issuance.

F. Documentation of the EQR

The repropoed standard required the EQR documentation to contain sufficient information to identify: who performed the review, the documents reviewed, whether and when concurring approval of issuance was provided or the reasons for not providing the approval, and the significant discussions held, including the details of such discussions. These provisions were intended to respond to comments expressing concern that the originally proposed documentation requirements were overly detailed and would result in duplication of the engagement team's work. Some commenters reiterated their concerns that some of the repropoed requirements were duplicative of requirements to document the engagement itself or overly burdensome.

The Board continues to believe that it is necessary to strengthen the documentation requirements in the interim standard to provide for an informative record of the work performed during the EQR. At the same time, the Board has reconsidered its approach to the documentation requirement in light of the comments received. As described below, the Board has added a general requirement that places the specific requirements in the context of the overall purpose of EQR documentation – to provide a record of how the reviewer carried out the review in accordance with the standard's requirements.

Specifically, paragraph 19 of AS No. 7 includes a requirement for the engagement documentation to contain sufficient information to enable an experienced auditor,^{28/} having no previous connection with the engagement, to understand the procedures performed by the engagement quality reviewer, and others who assisted the reviewer, to comply with the provisions of the standard.^{29/} This provision is similar to the audit documentation requirement in paragraph 6 of AS No. 3, and should clarify how the more specific requirements are meant to apply in particular circumstances.

^{28/} As described in paragraph 6 of AS No. 3, "[a]n experienced auditor has a reasonable understanding of audit activities and has studied the company's industry as well as the accounting and auditing issues relevant to the industry."

^{29/} Additionally, for clarity of presentation, the Board moved the requirement to include documentation of an EQR in the engagement documentation from paragraph 19 to a new paragraph 20 in AS No. 7.



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For example, if a reviewer identified a significant engagement deficiency to be addressed by the engagement team, the engagement team should document its response to the identified deficiency in accordance with AS No. 3. Because AS No. 7 does not require duplication of documentation prepared by the engagement team, the engagement quality reviewer does not have to separately document the engagement team's response. Rather, the EQR documentation should contain sufficient information to enable an experienced auditor, having no previous connection with the engagement, to understand, e.g., the significant deficiency identified, how the reviewer communicated the deficiency to the engagement team, why such matter was important, and how the reviewer evaluated the engagement team's response. Similarly, if the reviewer participated in the discussion of the potential for material misstatement due to fraud,^{30/} and the engagement team documented the discussion in accordance with AS No. 3, AS No. 7 only requires the engagement quality reviewer or reviewer's assistants to prepare separate documentation if the documentation prepared by the engagement team does not contain sufficient information to enable an experienced auditor, having no previous connection with the engagement, to understand the procedures performed by the engagement quality reviewer, and others who assisted the reviewer, to comply with the provisions of AS No. 7.

In response to comments, the Board also considered whether modifications were necessary to the specific requirements. First, the Board received several comments related to the provisions of repropoed paragraph 19.b, which required the EQR documentation to contain information sufficient to identify the documents reviewed. One commenter believed that a reviewer "may feel compelled to engage in an unnecessary review of additional documents in order to compile a more 'complete' list." Conversely, another commenter believed that the reviewer would be discouraged "to inspect one or more documents than he or she otherwise might or should, thus reducing the quality of the EQR." Some commenters suggested clarifying how the documents should be identified as "reviewed" (i.e., electronically or manually), or suggested limiting the scope of paragraph 19.b to "significant documents."

After considering these comments, the Board has decided to include this requirement in AS No. 7. Identifying a document as reviewed by the engagement quality reviewer should not be unduly burdensome, and will provide an informative record. Such a record could provide registered firms, and the Board, with better information about the EQR, which can be used to evaluate and improve the EQR process. The

^{30/} See paragraph .14 of AU sec. 316, *Consideration of Fraud in a Financial Statement Audit*.



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Board believes it is unnecessary to require in the standard a particular document identification method, such as electronic or manual signature. Rather, this should be determined by each firm individually.

Second, a number of commenters believed that the requirement in paragraph 19.c to document details of significant discussions held by the reviewer, and others who assisted the reviewer, would not improve audit quality and that it would be costly to implement. These commenters suggested that the reviewer might not be able to determine whether a discussion is significant at the time a discussion is held and therefore feel compelled to document every discussion. In order to make clear that documentation of every discussion is neither required nor a prudent use of resources, the Board has not included an explicit requirement to document discussions in AS No. 7. As explained above, however, if documentation of a particular discussion is necessary "to enable an experienced auditor, having no previous connection with the engagement, to understand the procedures performed . . . to comply with the provisions of th[e] standard," such documentation is required under the general documentation requirement.

G. Effective Date

In reproposing the standard, the Board intended to make a final standard effective for EQRs of interim reviews for fiscal years beginning after December 15, 2009 and for EQRs of audits for fiscal years ending on or after December 15, 2009. Several commenters were concerned that the proposed effective date would not allow for sufficient time to train the auditing firm's personnel and implement the new EQR requirements. These commenters recommended that the effective date of the EQR standard be linked to the beginning of an audit period to provide adequate time for registered firms to prepare for adoption. The Board agrees with the concerns expressed by the commenters and has decided to make AS No. 7 effective, subject to SEC approval, for both the EQR of audits and the EQR of interim reviews for fiscal years beginning on or after December 15, 2009.

H. Comparison with other EQR Standards

Three commenters suggested that the Board provide a comparison between the EQR standard and standards of other standard-setters on this subject. One commenter noted that because issuer clients often represent a minor part of a smaller firm's audit client base, the audit methodology of such a firm may be based on other standards as well as PCAOB standards. In response, the Board has described certain significant



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differences between the Board's EQR standard and the analogous standards of the International Auditing and Assurance Standards Board ("IAASB")^{31/} and the Auditing Standards Board ("ASB") of the AICPA^{32/} in Appendix 3. Each section of the appendix also includes references to the relevant paragraphs of AS No. 7.

Appendix 3 is provided for informational purposes only. It describes only certain provisions of AS No. 7, and is not a substitute for the EQR standard itself. The full text of AS No. 7 is included in Appendix 1 of this release. Compliance with AS No. 7 is required for registered public accounting firms. Compliance with the analogous ASB and IAASB standards is not sufficient to meet the requirements of AS No. 7.

* * *

^{31/} International Standard on Quality Control 1, *Quality Control for Firms that Perform Audits and Reviews of Financial Statements, and Other Assurance and Related Services Engagements*, and International Standard on Auditing 220, *Quality Control for an Audit of Financial Statements*, issued in December 2008.

^{32/} AICPA, Statement on Quality Control Standards No. 7, *A Firm's System of Quality Control* (October 2007).



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On the 28th day of July, in the year 2009, the foregoing was, in accordance with the bylaws of the Public Company Accounting Oversight Board,

ADOPTED BY THE BOARD.

/s/ J. Gordon Seymour

J. Gordon Seymour
Secretary

July 28, 2009

APPENDIX 1 – Auditing Standard No. 7 – *Engagement Quality Review*

APPENDIX 2 – Conforming Amendment to PCAOB Interim Quality Control Standards

APPENDIX 3 – Analysis of Significant Differences between the Requirements of Auditing Standard No. 7, *Engagement Quality Review*, of the Public Company Accounting Oversight Board and the Analogous Standards of the International Auditing and Assurance Standards Board, and the Auditing Standards Board of the American Institute of Certified Public Accountants



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Auditing Standard No. 7

Supersedes SECPS Requirements of Membership § 1000.08(f).

Engagement Quality Review

Applicability of Standard

1. An engagement quality review and concurring approval of issuance are required for each audit engagement and for each engagement to review interim financial information conducted pursuant to the standards of the Public Company Accounting Oversight Board ("PCAOB").

Objective

2. The objective of the engagement quality reviewer is to perform an evaluation of the significant judgments made by the engagement team and the related conclusions reached in forming the overall conclusion on the engagement and in preparing the engagement report, if a report is to be issued, in order to determine whether to provide concurring approval of issuance.^{1/}

Qualifications of an Engagement Quality Reviewer

3. The engagement quality reviewer must be an associated person of a registered public accounting firm. An engagement quality reviewer from the firm that issues the engagement report (or communicates an engagement conclusion, if no report is issued)

^{1/} In the context of an audit, "engagement report" refers to the audit report (or reports if, in an integrated audit, the auditor issues separate reports on the financial statements and internal control over financial reporting). In the context of an engagement to review interim financial information, the term refers to the report on interim financial information. An engagement report might not be issued in connection with a review of interim financial information. See paragraph .03 of AU section ("sec.") 722, *Interim Financial Information*.



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must be a partner or another individual in an equivalent position. The engagement quality reviewer may also be an individual from outside the firm.^{2/}

4. As described below, an engagement quality reviewer must have competence, independence, integrity, and objectivity.

Note: The firm's quality control policies and procedures should include provisions to provide the firm with reasonable assurance that the engagement quality reviewer has sufficient competence, independence, integrity, and objectivity to perform the engagement quality review in accordance with the standards of the PCAOB.

Competence

5. The engagement quality reviewer must possess the level of knowledge and competence related to accounting, auditing, and financial reporting required to serve as the engagement partner on the engagement under review.^{3/}

Independence, Integrity, and Objectivity

6. The engagement quality reviewer must be independent of the company, perform the engagement quality review with integrity, and maintain objectivity in performing the review.

^{2/} An outside reviewer who is not already associated with a registered public accounting firm would become associated with the firm issuing the report if *he or she* (rather than, or in addition to, his or her firm or other employer): (1) receives compensation from the firm issuing the report for performing the review or (2) performs the review as agent for the firm issuing the report. See PCAOB Rule 1001(p)(i) for the definition of an associated person of a registered public accounting firm.

^{3/} The term "engagement partner" has the same meaning as the phrases "auditor with final responsibility for the audit" in AU sec. 311, *Planning and Supervision*, and "practitioner-in-charge of an engagement" in PCAOB interim quality control standard QC sec. 40, *The Personnel Management Element of a Firm's System of Quality Control-Competencies Required by a Practitioner-in-Charge of an Attest Engagement*. QC sec. 40 describes the competencies required of a practitioner-in-charge of an attest engagement.



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Note: The reviewer may use assistants in performing the engagement quality review. Personnel assisting the engagement quality reviewer also must be independent, perform the assigned procedures with integrity, and maintain objectivity in performing the review.

7. To maintain objectivity, the engagement quality reviewer and others who assist the reviewer should not make decisions on behalf of the engagement team or assume any of the responsibilities of the engagement team. The engagement partner remains responsible for the engagement and its performance, notwithstanding the involvement of the engagement quality reviewer and others who assist the reviewer.

8. The person who served as the engagement partner during either of the two audits preceding the audit subject to the engagement quality review may not be the engagement quality reviewer. Registered firms that qualify for the exemption under Rule 2-01(c)(6)(ii) of Regulation S-X, 17 C.F.R. § 210.2-01(c)(6)(ii), are exempt from the requirement in this paragraph.

Engagement Quality Review for an Audit

Engagement Quality Review Process

9. In an audit engagement, the engagement quality reviewer should evaluate the significant judgments made by the engagement team and the related conclusions reached in forming the overall conclusion on the engagement and in preparing the engagement report. To evaluate such judgments and conclusions, the engagement quality reviewer should, to the extent necessary to satisfy the requirements of paragraphs 10 and 11: (1) hold discussions with the engagement partner and other members of the engagement team, and (2) review documentation.

10. In an audit, the engagement quality reviewer should:

- a. Evaluate the significant judgments that relate to engagement planning, including –
 - The consideration of the firm's recent engagement experience with the company and risks identified in connection with the firm's client acceptance and retention process,



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- The consideration of the company's business, recent significant activities, and related financial reporting issues and risks, and
 - The judgments made about materiality and the effect of those judgments on the engagement strategy.
- b. Evaluate the engagement team's assessment of, and audit responses to –
- Significant risks identified by the engagement team, including fraud risks, and
 - Other significant risks identified by the engagement quality reviewer through performance of the procedures required by this standard.

Note: A *significant risk* is a risk of material misstatement that is important enough to require special audit consideration.

- c. Evaluate the significant judgments made about (1) the materiality and disposition of corrected and uncorrected identified misstatements and (2) the severity and disposition of identified control deficiencies.
- d. Review the engagement team's evaluation of the firm's independence in relation to the engagement.
- e. Review the engagement completion document^{4/} and confirm with the engagement partner that there are no significant unresolved matters.
- f. Review the financial statements, management's report on internal control, and the related engagement report.

^{4/} Paragraph 13 of PCAOB Auditing Standard No. 3, *Audit Documentation*, requires the auditor to identify all significant findings or issues in an engagement completion document.



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- g. Read other information in documents containing the financial statements to be filed with the Securities and Exchange Commission ("SEC")^{5/} and evaluate whether the engagement team has taken appropriate action with respect to any material inconsistencies with the financial statements or material misstatements of fact of which the engagement quality reviewer is aware.
- h. Based on the procedures required by this standard, evaluate whether appropriate consultations have taken place on difficult or contentious matters. Review the documentation, including conclusions, of such consultations.
- i. Based on the procedures required by this standard, evaluate whether appropriate matters have been communicated, or identified for communication, to the audit committee, management, and other parties, such as regulatory bodies.

Evaluation of Engagement Documentation

11. In an audit, the engagement quality reviewer should evaluate whether the engagement documentation that he or she reviewed when performing the procedures required by paragraph 10 –

- a. Indicates that the engagement team responded appropriately to significant risks, and
- b. Supports the conclusions reached by the engagement team with respect to the matters reviewed.

^{5/} See paragraphs .04-.06 of AU sec. 550, *Other Information in Documents Containing Audited Financial Statements*; AU sec. 711, *Filings Under Federal Securities Statutes*.



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Concurring Approval of Issuance

12. In an audit, the engagement quality reviewer may provide concurring approval of issuance only if, after performing with due professional care^{6/} the review required by this standard, he or she is not aware of a significant engagement deficiency.

Note: A *significant engagement deficiency* in an audit exists when (1) the engagement team failed to obtain sufficient appropriate evidence in accordance with the standards of the PCAOB, (2) the engagement team reached an inappropriate overall conclusion on the subject matter of the engagement, (3) the engagement report is not appropriate in the circumstances, or (4) the firm is not independent of its client.

13. In an audit, the firm may grant permission to the client to use the engagement report only after the engagement quality reviewer provides concurring approval of issuance.^{7/}

Engagement Quality Review for a Review of Interim Financial Information

Engagement Quality Review Process

14. In an engagement to review interim financial information, the engagement quality reviewer should evaluate the significant judgments made by the engagement team and the related conclusions reached in forming the overall conclusion on the engagement and in preparing the engagement report, if a report is to be issued. To evaluate such judgments and conclusions, the engagement quality reviewer should, to the extent necessary to satisfy the requirements of paragraphs 15 and 16: (1) hold discussions

^{6/} See AU sec. 230, *Due Professional Care in the Performance of Work*.

^{7/} Concurring approval of issuance by the engagement quality reviewer also is required when reissuance of an engagement report requires the auditor to update his or her procedures for subsequent events. In that case, the engagement quality reviewer should update the engagement quality review by addressing those matters related to the subsequent events procedures.



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with the engagement partner and other members of the engagement team, and (2) review documentation.

15. In a review of interim financial information, the engagement quality reviewer should:

- a. Evaluate the significant judgments that relate to engagement planning, including the consideration of –
 - The firm's recent engagement experience with the company and risks identified in connection with the firm's client acceptance and retention process,
 - The company's business, recent significant activities, and related financial reporting issues and risks, and
 - The nature of identified risks of material misstatement due to fraud.
- b. Evaluate the significant judgments made about (1) the materiality and disposition of corrected and uncorrected identified misstatements and (2) any material modifications that should be made to the disclosures about changes in internal control over financial reporting.
- c. Perform the procedures described in paragraphs 10.d and 10.e.
- d. Review the interim financial information for all periods presented and for the immediately preceding interim period, management's disclosure for the period under review, if any, about changes in internal control over financial reporting, and the related engagement report, if a report is to be issued.
- e. Read other information in documents containing interim financial information to be filed with the SEC^{8/} and evaluate whether the engagement team has taken appropriate action with respect to material inconsistencies with the interim financial information or material misstatements of fact of which the engagement quality reviewer is aware.

^{8/} See AU sec. 722.18f; AU sec. 711.



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- f. Perform the procedures in paragraphs 10.h and 10.i

Evaluation of Engagement Documentation

16. In a review of interim financial information, the engagement quality reviewer should evaluate whether the engagement documentation that he or she reviewed when performing the procedures required by paragraph 15 supports the conclusions reached by the engagement team with respect to the matters reviewed.

Concurring Approval of Issuance

17. In a review of interim financial information, the engagement quality reviewer may provide concurring approval of issuance only if, after performing with due professional care the review required by this standard, he or she is not aware of a significant engagement deficiency.

Note: A *significant engagement deficiency* in a review of interim financial information exists when (1) the engagement team failed to perform interim review procedures necessary in the circumstances of the engagement, (2) the engagement team reached an inappropriate overall conclusion on the subject matter of the engagement, (3) the engagement report is not appropriate in the circumstances, or (4) the firm is not independent of its client.

18. In a review of interim financial information, the firm may grant permission to the client to use the engagement report (or communicate an engagement conclusion to its client, if no report is issued) only after the engagement quality reviewer provides concurring approval of issuance.



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Documentation of an Engagement Quality Review

19. Documentation of an engagement quality review should contain sufficient information to enable an experienced auditor, having no previous connection with the engagement, to understand the procedures performed by the engagement quality reviewer, and others who assisted the reviewer, to comply with the provisions of this standard, including information that identifies:

- a. The engagement quality reviewer, and others who assisted the reviewer,
- b. The documents reviewed by the engagement quality reviewer, and others who assisted the reviewer,
- c. The date the engagement quality reviewer provided concurring approval of issuance or, if no concurring approval of issuance was provided, the reasons for not providing the approval.

20. Documentation of an engagement quality review should be included in the engagement documentation.

21. The requirements related to retention of and subsequent changes to audit documentation in PCAOB Auditing Standard No. 3, *Audit Documentation*, apply with respect to the documentation of the engagement quality review.



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Conforming Amendment to PCAOB Interim Quality Control Standards

QC sec. 20, "System of Quality Control for a CPA Firm's Accounting and Auditing Practice"

QC section ("sec.") 20, "System of Quality Control for a CPA Firm's Accounting and Auditing Practice" of the Board's interim quality control standards is amended as follows –

The third sentence of paragraph .18 of QC sec. 20 is replaced with the following sentence:

These policies and procedures also should address engagement quality reviews pursuant to PCAOB Auditing Standard No. 7, *Engagement Quality Review*.



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Analysis of Significant Differences between the Requirements of Auditing Standard No. 7, *Engagement Quality Review*, of the Public Company Accounting Oversight Board and the Analogous Standards of the International Auditing and Assurance Standards Board, and the Auditing Standards Board of the American Institute of Certified Public Accountants

Introduction

This appendix includes an analysis of significant differences between Auditing Standard No. 7, *Engagement Quality Review* ("AS No. 7" or the "EQR standard") of the Public Company Accounting Oversight Board ("PCAOB"), and the analogous standards of the Auditing Standards Board ("ASB") of the American Institute of Certified Public Accountants ("AICPA"),^{1/} and the International Auditing and Assurance Standards Board ("IAASB").^{2/} This analysis may not represent the views of the ASB or IAASB regarding the interpretation of their standards.

Appendix 3 is provided for informational purposes only. It describes only certain provisions of AS No. 7, and is not a substitute for the standard itself. The full text of AS No. 7 is included in Appendix 1 of this release. Compliance with AS No. 7 is required for registered public accounting firms. Compliance with the analogous ASB and IAASB standards is not sufficient to meet the requirements of AS No. 7.

The Board has developed AS No. 7 to enhance the quality of the engagement quality review ("EQR") process by strengthening the provisions of the Board's interim standard.^{3/} Recently, the ASB and IAASB also updated their standards related to the EQR, and the Board considered information in the standards of the ASB and IAASB

^{1/} AICPA, Statement on Quality Control Standards No. 7 ("SQCS No. 7"), *A Firm's System of Quality Control* (October 2007).

^{2/} International Standard on Quality Control 1 ("ISQC 1"), *Quality Control for Firms that Perform Audits and Reviews of Financial Statements, and Other Assurance and Related Services Engagements*, and International Standard on Auditing 220 ("ISA 220"), *Quality Control for an Audit of Financial Statements*, issued in December 2008.

^{3/} The Securities and Exchange Commission Practice Section ("SECPS") of the AICPA Requirements of Membership Sections 1000.08(f); 1000.39, Appendix E.



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when developing its new EQR standard. As described in this appendix, AS No. 7 includes provisions that are similar in terminology and substance to those in the ASB and IAASB standards, and other provisions added as necessary by the Board. For example, the Board included certain provisions in AS No. 7 that are not included in the standards of the ASB or IAASB to: comply with the requirements of the Sarbanes-Oxley Act ("the Act"); respond to the feedback received on the interim standard from the Board's Standing Advisory Group ("SAG") and information obtained through PCAOB oversight of registered firms; and to ensure consistency of the provisions of AS No. 7 with the provisions and terminology of other relevant standards of the PCAOB.

Some of the provisions of the IAASB standards described in this appendix are included in the "Application and Other Explanatory Material" section of these standards. That section "does not in itself impose a requirement," but "is relevant to the proper application of the requirements of an ISA."^{4/} In contrast, the comparable provisions of AS No. 7 are included in the standard, and establish requirements.

Applicability

PCAOB

Section 103 of the Act requires the Board to adopt an EQR standard for audit engagements.^{5/} Because of the importance of interim financial information to investors, the Board has decided to include a requirement to perform an EQR for reviews of interim financial information performed in accordance with AU section ("sec.") 722, *Interim Financial Information*, ("interim reviews") in the EQR standard. Accordingly, AS No. 7 requires an EQR and concurring approval of issuance for each audit engagement and for each interim review engagement conducted pursuant to the standards of the PCAOB.^{6/}

^{4/} See paragraph A59 of ISA 200, *Overall Objectives of the Independent Auditor and the Conduct of an Audit in Accordance with International Standards on Auditing*.

^{5/} See Section 103(a)(2)(A)(ii) of the Act.

^{6/} See paragraph 1 of AS No. 7.



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ASB

SQCS No. 7 does not require an EQR for any type of engagement. Accounting firms should determine whether an EQR is required for any engagement.^{7/}

IAASB

ISQC 1 requires an EQR only for audits of financial statements of listed entities. Accounting firms should determine whether an EQR is required for any other engagements.^{8/}

Qualifications of a Reviewer

PCAOB

Associated Person – In order to obtain cooperation with the Board of the individuals that perform an EQR,^{9/} the Board included in AS No. 7 a requirement, according to which the engagement quality reviewer must be an associated person of a registered public accounting firm.^{10/}

A Reviewer from Outside the Firm – Similar to the standards of the ASB and IAASB,^{11/} AS No. 7 allows a qualified individual from outside the firm to perform an EQR.^{11/}

^{7/} See paragraphs 80-81 and 83 of SQCS No. 7.

^{8/} See paragraphs 35(a)-(b) of ISQC 1.

^{9/} A registered public accounting firm has an obligation to secure and enforce consents to cooperate with the Board from each associated person of the firm, see Section 102(b)(3) of the Act, including those who become associated with the firm by performing the review. The Board also may directly sanction any such person who fails to cooperate in an investigation or inspection. See Section 105(b)(3) of the Act and PCAOB Rules 5110 and 4006.

^{10/} See paragraph 3 of AS No. 7.

^{11/} See id.



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Partner or Person in an Equivalent Position – Because the EQR is intended to be an objective "second look" at work performed by the engagement team, the reviewer should possess sufficient authority to be able to withstand pressure from the engagement partner or other firm personnel, such as members of the firm's national office. The Board believes that concerns about authority will most often arise when the reviewer and the engagement partner are from the same firm. Therefore, the Board included in AS No. 7 the requirement that an in-house reviewer – but not one from outside the firm – be a partner or another individual in an equivalent position.^{12/}

General Competence Requirement – The Board included in AS No. 7 a requirement for the reviewer to possess the level of knowledge and competence related to accounting, auditing, and financial reporting required to serve as the engagement partner on the engagement under review.^{13/} Without such knowledge and competence, the reviewer would not be able to appropriately evaluate the significant judgments made and related conclusions reached by the engagement team in an audit or an interim review.

Independence, Integrity, and Objectivity – The reviewer must comply with all applicable independence requirements,^{14/} and perform the review with integrity and objectivity.^{15/} The engagement quality reviewer should be able to take a step back and conduct the review from the perspective of an outsider looking in.

Accordingly, AS No. 7 requires that the firm's quality control policies and procedures should include provisions to provide the firm with reasonable assurance that the engagement quality reviewer has sufficient competence, independence, integrity,

^{12/} See *id.*

^{13/} See paragraph 5 of AS No. 7. PCAOB interim quality control standards describe the competencies required of a person who has the overall responsibility for an engagement (or any practitioner-in-charge of an attest engagement). See QC sec. 40, *The Personnel Management Element of a Firm's System of Quality Control-Competencies Required by a Practitioner-in-Charge of an Attest Engagement*.

^{14/} See, e.g., Rule 2-01(c)(6) of Regulation S-X, 17 C.F.R. § 210.2-01(c)(6) (subjecting the engagement quality reviewer to the five-year partner rotation requirement).

^{15/} See ET sec. 102, *Integrity and Objectivity*, and ET sec. 191, *Ethics Rulings on Independence, Integrity, and Objectivity*.



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and objectivity to perform the engagement quality review in accordance with the standards of the PCAOB.^{16/} As described later, the ASB and IAASB contain similar provisions, except the standards of IAASB do not include the direction on independence for the reviewer.

While AS No. 7 does not contain the direction included in the standards of ASB and IAASB that the firm's policies and procedures should establish the degree to which a reviewer can be consulted on the engagement without compromising his or her objectivity,^{17/} or provide for the replacement of the reviewer when the reviewer's ability to perform an objective review has been, or may be, impaired,^{18/} such direction is implicit in the requirement of AS No. 7 that a reviewer must maintain objectivity in performing the EQR.^{19/} Importantly, AS No. 7 provides direction on maintaining objectivity, according to which the engagement quality reviewer and others who assist the reviewer should not make decisions on behalf of the engagement team or assume any of the responsibilities of the engagement team.^{20/}

"Cooling-off" period – An engagement quality reviewer is expected to take a fresh, objective look at the engagement. The Board believes that it would be harder for an engagement partner, who has had overall responsibility for the audit for a year or more, to perform the EQR with the necessary level of objectivity. Accordingly, AS No. 7 includes a requirement, according to which the reviewer may not be the person who served as the engagement partner during either of the two audits preceding the audit subject to the EQR. (Registered firms that qualify for the exemption under Rule 2-01(c)(6)(ii) of Regulation S-X, 17 C.F.R. § 210.2-01(c)(6)(ii), are exempt from this requirement.)^{21/}

^{16/} See paragraph 4 of AS No. 7.

^{17/} See paragraph 96 of SQCS No.7; paragraph 39(b) of ISQC 1.

^{18/} See paragraph 97 of SQCS No. 7; paragraph 41 of ISQC 1.

^{19/} See paragraph 6 of AS No. 7.

^{20/} See paragraph 7 of AS No. 7.

^{21/} See paragraph 8 of AS No. 7.



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ASB

SQCS No. 7 requires an auditing firm to establish the engagement quality reviewer qualifications, including those related to experience, authority, and objectivity.^{22/} SQCS No. 7 describes the engagement quality reviewer as a partner, other person in the firm, qualified external person, or a team made up of such individuals, none of whom is part of the engagement team, with sufficient and appropriate experience and authority to perform the EQR.^{23/} According to SQCS No. 7, what constitutes sufficient and appropriate technical experience, and authority depends on the circumstances of the engagement.^{24/}

SQCS No. 7 does not include a "cooling-off" period, or a requirement for the reviewer to be an associated person of a registered public accounting firm.

Similar to AS No. 7, SQCS No. 7 requires that the firm establish policies and procedures designed to maintain the objectivity of the reviewer, and that such policies and procedures provide that the reviewer should satisfy the independence requirements relating to the engagements reviewed.^{25/} Unlike AS No. 7, SQCS No. 7 does not provide a specific direction on maintaining objectivity. Instead, SQCS No. 7 provides examples of policies and procedures for maintaining the objectivity of the reviewer.^{26/}

IAASB

ISQC 1 requires an auditing firm to establish the engagement quality reviewer qualification requirements, including those related to experience, authority, and objectivity.^{27/} The engagement quality reviewer is described as a partner, other person in the firm, suitably qualified external person, or a team made up of such individuals, none of whom is part of the engagement team, with sufficient and appropriate experience and authority to objectively evaluate the significant judgments the

^{22/} See paragraphs 92-94 of SQCS No. 7.

^{23/} See paragraph 5.e of SQCS No. 7.

^{24/} See paragraph 93 of SQCS No. 7.

^{25/} See paragraph 94 of SQCS No. 7.

^{26/} See paragraph 95 of SQCS No. 7.

^{27/} See paragraphs 39 and 40 of ISQC 1.



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engagement team made and the conclusions it reached in formulating the report.^{28/} The application materials in ISQC 1 state that what constitutes sufficient and appropriate technical expertise, experience and authority depends on the circumstances of the engagement.^{29/}

ISQC 1 and ISA 220 do not include reviewer independence or "cooling-off" requirements, or a requirement for the reviewer to be an associated person of a registered public accounting firm.

Similar to AS No. 7, ISQC 1 requires that the firm establish policies and procedures designed to maintain the objectivity of the reviewer.^{30/} Unlike AS No. 7, the IAASB standards do not provide specific direction on maintaining objectivity. Instead, the application materials of ISQC 1 discuss policies and procedures for maintaining the objectivity of the reviewer.^{31/}

Engagement Quality Review for an Audit

Engagement Quality Review Process

PCAOB

Similar to the standards of the ASB and IAASB, AS No. 7 requires the reviewer to evaluate the significant judgments made and the related conclusions reached by the engagement team in forming the overall conclusion on the engagement and in preparing the engagement report; and to carry out the review through discussions with those performing the engagement and the review of documentation.^{32/}

^{28/} See paragraph 12(e) of ISQC 1; paragraph 7(c) of ISA 220.

^{29/} See paragraph A47 of the Application and Other Explanatory Materials of ISQC 1.

^{30/} See paragraph 40 of ISQC 1.

^{31/} See paragraph A49 of the Application and Other Explanatory Materials of ISQC 1.

^{32/} See paragraph 9 of AS No. 7.



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Further, AS No. 7 specifically requires the reviewer, among other things, to evaluate:

- The significant judgments that relate to engagement planning;^{33/}
- The engagement team's assessment of and audit responses to significant risks, including fraud risks;^{34/} and
- The significant judgments made about identified misstatements and control deficiencies.^{35/}

Also, AS No. 7 contains a requirement, similar to a requirement for audits of listed entities in ISA 220, according to which the reviewer, based on the procedures required by the standard, should evaluate whether appropriate consultations have taken place on difficult or contentious matters, and review the documentation, including conclusions, of such consultations.^{36/}

According to PCAOB Rule 3520, *Auditor Independence*, "[a] registered public accounting firm and its associated persons must be independent of the firm's audit client throughout the audit and professional engagement period." Because of the importance of compliance with PCAOB and Securities and Exchange Commission ("SEC") independence requirements, AS No. 7 requires the reviewer to review the engagement team's evaluation of the firm's independence in relation to the engagement.^{37/}

In 2004, the Board adopted Auditing Standard No. 3, *Audit Documentation* ("AS No. 3"). According to paragraph 13 of AS No. 3, the auditor must identify all significant findings or issues in an engagement completion document. AS No. 7 requires the reviewer to review the engagement completion document and confirm with the person

^{33/} See paragraph 10.a of AS No. 7.

^{34/} See paragraph 10.b of AS No. 7.

^{35/} See paragraph 10.c of AS No. 7.

^{36/} See paragraph 10.h of AS No. 7.

^{37/} See paragraph 10.d of AS No. 7.



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who has overall responsibility for the engagement that there are no significant unresolved matters.^{38/}

Similar to the standards of the ASB and IAASB, AS No. 7 requires the reviewer to review the financial statements and the related engagement report.^{39/} Additionally, because an integrated audit includes an audit of internal control over financial reporting,^{40/} AS No. 7 requires the reviewer to review management's report on internal control.^{41/}

An issuer may publish various documents that contain information in addition to audited financial statements and the auditor's report thereon. The auditor is required to read the other information and consider whether such information, or the manner of its presentation, is materially inconsistent with information, or the manner of its presentation, appearing in the financial statements.^{42/} Accordingly, AS No. 7 requires the reviewer to read other information in documents containing the financial statements to be filed with the SEC and evaluate whether the engagement team has taken appropriate action with respect to any material inconsistencies with the financial statements or material misstatements of fact of which the engagement quality reviewer is aware.^{43/}

Finally, because of the importance to the audit process of effective communication between the auditor and those charged with governance, AS No. 7 requires the reviewer, based on the procedures required by the standard, to evaluate

^{38/} See paragraph 10.e of AS No. 7.

^{39/} See paragraph 10.f of AS No. 7.

^{40/} PCAOB Auditing Standard No. 5, *An Audit of Internal Control Over Financial Reporting That Is Integrated with An Audit of Financial Statements* establishes requirements and provides direction that apply when an auditor is engaged to perform an audit of management's assessment of the effectiveness of internal control over financial reporting.

^{41/} See paragraph 10.f of AS No. 7.

^{42/} See AU sec. 550, *Other Information in Documents Containing Audited Financial Statements*.

^{43/} See paragraph 10.g of AS No. 7.



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whether appropriate matters have been communicated, or identified for communication, to the audit committee, management, and other parties, such as regulatory bodies.^{44/}

ASB

Similar to AS No. 7, SQCS No. 7 requires that the EQR procedures include an objective evaluation of the significant judgments made by the engagement team and the conclusions reached in formulating the report.^{45/} The EQR performed in accordance with SQCS No. 7 should include: reading the financial statements or other subject matter information and the report and considering whether the report is appropriate; review of selected documentation; and a discussion with the engagement partner regarding significant findings and issues.^{46/}

In addition to the required procedures summarized in the preceding paragraph, an EQR performed in accordance with SQCS No. 7 may include consideration of certain other matters, examples of which are provided in the standard. SQCS No. 7 also provides examples of significant judgments that could be made by the engagement team.^{47/}

IAASB

The EQR procedures required by the standards of the IAASB are similar to those required by the ASB.^{48/} Additionally, for audits of listed entities, the IAASB standards require the reviewer to consider: the engagement team's evaluation of the firm's independence in relation to the engagement; and whether appropriate consultation has taken place on matters involving differences of opinion or other difficult or contentious matters, and the conclusions arising from those consultations.^{49/}

^{44/} See paragraph 10.i of AS No. 7.

^{45/} See paragraph 85 of SQCS No. 7.

^{46/} See paragraphs 86 and 87 of SQCS No. 7.

^{47/} See paragraphs 88 and 89 of SQCS No. 7.

^{48/} See paragraph 37 of ISQC 1; paragraph 20 of ISA 220.

^{49/} See paragraphs 38(a) and 38(b) of ISQC 1; paragraphs 21(a) and 21(b) of ISA 220.



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Evaluation of Engagement Documentation

PCAOB

AS No. 7 includes a documentation review requirement that is similar to the requirement for audits of listed entities in the IAASB standards. According to AS No. 7, the reviewer should evaluate whether the engagement documentation that he or she reviewed when performing the required EQR procedures indicates that the engagement team responded appropriately to significant risks and supports the conclusions reached by the engagement team with respect to the matters reviewed.^{50/}

ASB

Unlike AS No. 7, SQCS No. 7 does not require the reviewer to evaluate whether the engagement documentation satisfies certain criteria. Instead, SQCS No. 7 states that an EQR may include consideration of whether working papers selected for review reflect the work performed in relation to the significant judgments and support the conclusions reached.^{51/}

IAASB

Similar to AS No. 7, the IAASB standards require, for audits of financial statements of listed entities, that the reviewer consider whether audit documentation selected for review reflects the work performed in relation to the significant judgments and supports the conclusions reached.^{52/}

Concurring Approval of Issuance and Resolution of Differences of Opinion

PCAOB

Under the Act,^{53/} the Board's standard on EQR must require concurring approval of issuance of each audit report. AS No. 7 states that the engagement quality reviewer

^{50/} See paragraph 11 of AS No. 7.

^{51/} See paragraph 88 of SQCS No. 7.

^{52/} See paragraph 38(c) of ISQC 1; paragraph 21(c) of ISA 220.

^{53/} See Section 103(a)(2)(A)(ii) of the Act.



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may provide concurring approval of issuance only if, after performing with due professional care the review required by the standard, he or she is not aware of a significant engagement deficiency.^{54/} The firm may grant permission to the client to use the engagement report only after the engagement quality reviewer provides concurring approval of issuance.^{55/}

Unlike the standards of the ASB and IAASB, AS No. 7 does not include an explicit provision for addressing differences of opinion. Firms may develop their own procedures for resolving such differences. Ultimately, however, under the standard, the reviewer may not provide concurring approval of issuance if there remains a significant engagement deficiency. If no concurring approval is provided, AS No. 7 requires that the EQR documentation include information that identifies the reasons for not providing the approval.

ASB

SQCS No. 7 does not include a requirement for the engagement quality reviewer to provide concurring approval of issuance. Instead, SQCS No. 7 requires the EQR be completed before the engagement report is released.^{56/} According to SQCS No. 7, when the engagement quality reviewer makes recommendations that the engagement partner does not accept and the matter is not resolved to the reviewer's satisfaction, the firm's procedures for dealing with differences of opinion apply.^{57/} The firm's policies and procedures should require that conclusions reached be documented and implemented, and the engagement report not be released until the matter, on which the difference of opinion has arisen, is resolved.^{58/}

^{54/} According to paragraph 12 of AS No. 7, "A *significant engagement deficiency* in an audit exists when (1) the engagement team failed to obtain sufficient appropriate evidence in accordance with the standards of the PCAOB, (2) the engagement team reached an inappropriate overall conclusion on the subject matter of the engagement, (3) the engagement report is not appropriate in the circumstances, or (4) the firm is not independent of its client."

^{55/} See paragraph 13 of AS No. 7.

^{56/} See paragraph 81 of SQCS No. 7.

^{57/} See paragraph 91 of SQCS No. 7.

^{58/} See paragraph 78 of SQCS No. 7.



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IAASB

The standards of the IAASB do not include a requirement for the engagement quality reviewer to provide concurring approval of issuance. Instead, the IAASB standards require that the engagement partner should not date the auditor's report until the completion of the EQR.^{59/} If differences of opinion arise between the engagement partner and the engagement quality reviewer, ISA 220 requires the engagement team to follow the firm's policies and procedures for dealing with and resolving differences of opinion.^{60/} ISQC 1 requires the firm to establish policies and procedures for dealing with and resolving differences of opinion between the engagement partner and the engagement quality reviewer. Such policies and procedures shall require that conclusions reached be documented and implemented, and the report not be dated until the matter is resolved.^{61/}

Documentation of an EQR

PCAOB

Because of deficiencies in the documentation of concurring reviews, the Board decided to strengthen the existing documentation requirements. AS No. 7 requires that documentation of an EQR should contain sufficient information to enable an experienced auditor, having no previous connection with the engagement, to understand the procedures performed by the engagement quality reviewer, and others who assisted the reviewer, to comply with the provisions of the standard, including information that identifies: the engagement quality reviewer, and others who assisted the reviewer; the documents reviewed by the engagement quality reviewer and others who assisted the reviewer; and the date the engagement quality reviewer provided concurring approval of issuance or, if no concurring approval of issuance was provided, the reasons for not providing the approval.^{62/}

^{59/} See paragraph 36 of ISQC 1; paragraph 19(c) of ISA 220.

^{60/} See paragraph 22 of ISA 220.

^{61/} See paragraphs 43-44 of ISQC 1.

^{62/} See paragraph 19 of AS No. 7.



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Unlike the standards of the ASB or the IAASB, AS No. 7 requires that the documentation of an EQR be included in the engagement documentation and provides requirements related to retention of and subsequent changes to the EQR documentation.^{63/}

ASB

According to SQCS No. 7, the documentation of an EQR should state that the procedures required by the firm's policies on EQR have been performed, the EQR has been completed before the report is released, and 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.^{64/}

SQCS No. 7 requires that the firm should: establish procedures designed to maintain the confidentiality, safe custody, integrity, accessibility, and retrievability of engagement documentation; and establish policies and procedures for the retention of engagement documentation for a period sufficient to meet the needs of the firm, professional standards, laws, and regulations.^{65/}

IAASB

The engagement quality reviewer is required to document that the procedures required by the firm's policies on the EQR have been performed, the EQR has been completed on or before the date of the auditor's report, and 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.^{66/}

ISQC 1 requires that the firm should establish policies and procedures related to the completion of the assembly of final engagement files; confidentiality, safe custody,

^{63/} See paragraphs 20-21 of AS No. 7.

^{64/} See paragraph 99 of SQCS No. 7.

^{65/} See paragraphs 63-71 of SQCS No. 7.

^{66/} See paragraph 42 of ISQC 1; paragraph 25 of ISA 220.



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integrity, accessibility and retrievability of engagement documentation; and retention of engagement documentation.^{67/}

^{67/} See paragraphs 45-47 of ISQC 1.