

# New PCAOB Auditing Standard to be Implemented Soon

The Public Company Accounting Oversight Board (PCAOB) has issued guidance intended to eliminate potential significant engagement deficiencies before report issuance. Auditing Standard No. 7, “[Engagement Quality Review](#)” (AS 7 or EQR), was adopted by the PCAOB on July 28, 2009, and, subject to approval of the U.S. Securities and Exchange Commission, will be effective for the EQRs of audits and the EQRs of interim reviews for fiscal years that begin on or after Dec. 15, 2009.

Many, but not all, audit firms previously performed a concurring partner review prior to issuing their audit report.<sup>1</sup> AS 7 will supersede, expand, and strengthen the previous practice for issuer audits by establishing specific guidance for the performance and documentation on an EQR of audits and interim review engagements that are performed in conformity with the standards of the PCAOB.

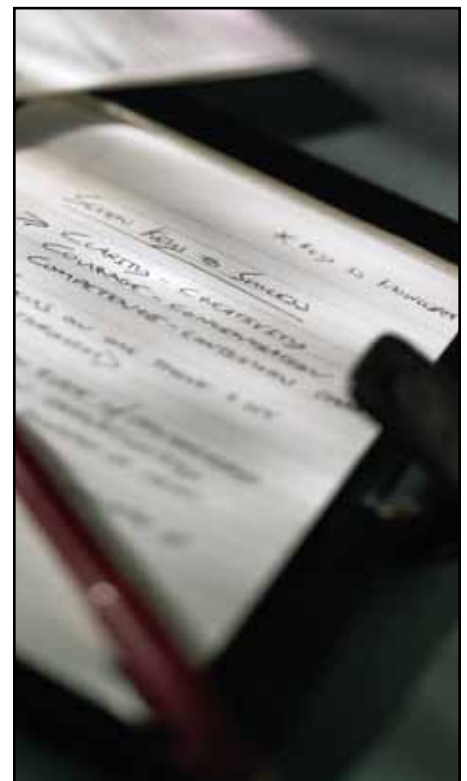
AS 7 states that the objective of the EQR is “to perform an evaluation of the significant judgments made by the engagement team and the related conclusions reached in forming the overall conclusion on the engagement and in preparing the engagement report, if a report is to be issued, in order to determine whether to provide concurring approval of issuance.” Following are some of the requirements the new rules impose in order to attain this objective.

## Qualifications of the Reviewer

AS 7 describes the qualifications a reviewer must have to perform a high-quality EQR. An engagement quality reviewer must:

- Possess the same level of knowledge and competence related to accounting, auditing, and financial reporting that is required to serve as the partner on the engagement; and
- Be independent of the company being audited, perform the EQR with integrity, and maintain objectivity. The reviewer should not assume any of the responsibilities of or make any decisions on behalf of the engagement team.

The engagement partner is prohibited from serving as the engagement quality reviewer for a period of at least two years after his or her last year as the engagement partner; this requirement



is in addition to the usual required rotation for the engagement. Some smaller firms are not required to comply with this new quality control enhancement.

## The EQR Process

Through discussion with members of the engagement team and a review of engagement documentation, the reviewer must evaluate significant judgments made by the engagement team and related conclusions the team reached when forming its overall conclusion about the engagement and preparing the engagement report. The standard identified specific procedures to be performed as a part of the EQR. Separate procedures are prescribed for reviewing audits and interim reviews, and all the procedures have been designed to give the reviewer the information necessary to evaluate the engagement team's judgments and conclusions.

For an audit, the required procedures focus on identifying and responding to significant risks – that is, risks of material misstatement that are important enough to require special audit consideration. The reviewer must determine whether the engagement documentation indicates that the engagement team responded appropriately to significant risks, and whether it supports the conclusions the team reached with respect to the matters reviewed. AS 7 also establishes a new requirement that the reviewer update the EQR by addressing matters related to subsequent events procedures when the engagement report must be reissued.

An EQR of an interim review of financial information is a new requirement that was not addressed in previous interim quality control practices. The requirements for

interim reviews are separate from the requirements for an EQR of an audit. Although very similar to the audit requirements, they are tailored specifically to the different procedures performed for an interim review.

When performing the EQR, the reviewer is expected to exercise “due professional care,” which has the same meaning as that described in AU Sec. 230 of the auditing standards – that is, reasonable care and diligence.

## Concurring Approval of Issuance

The reviewer can give concurring approval of issuance only if he or she is not aware of significant engagement deficiency. A significant engagement deficiency exists when:

- In an audit, the engagement team failed to obtain sufficient appropriate evidence in accordance with the standards of the PCAOB, or in a review of interim financial information, the engagement team failed to perform the interim review procedures necessary in the circumstances of the engagement;
- The engagement team reached an inappropriate overall conclusion on the subject matter of the engagement;
- The engagement report is not appropriate in the circumstances; or
- The audit firm is not independent of the client.

Only after the engagement quality reviewer provides concurring approval of issuance may the firm grant permission to the client to use the engagement report (or, if no report is issued, to communicate an engagement conclusion to the client).

## Documentation of an EQR

The audit firm's documentation of an EQR will contain sufficient information to enable an experienced auditor with no previous connection with the engagement to understand the procedures the reviewer performed. This documentation will identify the reviewer, the documents he or she reviewed, and the date he or she provided concurring approval of issuance. If the reviewer provided no concurring approval of issuance, the documentation will explain why. The requirements related to the retention of and subsequent changes to audit documentation in PCAOB Auditing Standard No. 3, “Audit Documentation,” apply to the documentation of the EQR.

## Summary

The provisions of AS 7 will need to be applied to engagement quality reviews of audits and interim reviews for fiscal years beginning on or after Dec. 15, 2009. Compliance with the new rules should provide a meaningful review of the work performed by the engagement team and serve as a safeguard against insufficiently supported audit opinions. In addition, the EQR requirement for interim reviews is a new requirement, so issuers and auditors need to plan for the additional time required for completing those new procedures.

## Contact Information

Wes Williams is a partner with Crowe Horwath LLP in the South Bend, Ind., office. He can be reached at [wes.williams@crowehorwath.com](mailto:wes.williams@crowehorwath.com) or 574.236.8626.

<sup>1</sup> Crowe Horwath LLP, as a voluntary adopter of the more stringent concurring review quality control practice, has performed concurring reviews.