

AUDITING STANDARD NO. 7 – Engagement Quality Review

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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) 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.

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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.

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.

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- 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.

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

^{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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- 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.

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

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

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.