



July 5, 2016

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

Grant Thornton LLP  
Grant Thornton Tower  
171 N. Clark Street, Suite 200  
Chicago, IL 60601-3370

T +1 312 856 0200  
F +1 312 565 4719  
grantthornton.com

Via Email to [comments@pcaobus.org](mailto:comments@pcaobus.org)

**Re: Request for Comment 2016-01, *Post-Implementation Review of Auditing Standard No. 7, Engagement Quality Review***

Dear Board Members and Staff:

Grant Thornton LLP appreciates the opportunity to respond to the Public Company Accounting Oversight Board's (PCAOB or Board) request for comment on the *Post-Implementation Review of Auditing Standard No. 7, Engagement Quality Review (AS 7)*. We support the Board's post-implementation review program and value the opportunity to provide feedback as part of this important process. We respectfully submit the following responses to certain of the questions posed in the Request for Comment.

**Question 1: Has AS 7 accomplished its intended purpose? In particular, has the implementation of AS 7 increased the likelihood that a registered public accounting firm will detect significant engagement deficiencies before the audit report is issued? Do engagement quality reviews performed under AS 7 provide for a meaningful check on the audit work performed by the engagement team?**

We believe that the adoption of AS 7 has improved upon the previous "concurring review" model and has positively impacted overall audit quality by providing more precise expectations for the engagement quality review (EQR) function and asserting the EQR's objectivity and need to operate independently from the engagement team. We believe the EQR process as enhanced by AS 7, when performed appropriately, increases the likelihood of detecting significant engagement deficiencies (SEDs) prior to report issuance and provides a meaningful assessment of the sufficiency of the audit work, conclusions on independence, and the appropriate form of report.

We have noted, however, that firms, in particular the larger firms, have been implementing processes to support and/or review engagement team work at various stages of the audit, including specialists in controls work, valuation, and other special skills area. Often these reviews are performed by national office or other persons not directly associated with the engagement. We note that such reviews are often focused on areas of quality risks, including the application of

new standards or where inspection issues have been noted. As we note below in our response to Question 6, we believe it would be helpful for the Board to continue to evaluate how such firm actions are impacting— or should impact—the EQR partner’s review.

**Question 3: What have been auditors’ experiences with implementation of AS 7? How did the implementation of AS 7 change practice? Has the implementation of AS 7 given rise to any unintended consequences or changes?**

*Experience*

In general, the auditor’s experience with the implementation of AS7 has been positive. Prior to the issuance of AS 7, there was less specificity as to the areas requiring review, which could have resulted in inefficient time being spent on areas of lesser risk. The introduction of AS 7 furthered the application of a “risk-based approach” to the review function.

However, EQR partners execute their reviews using various approaches, which are generally driven by individual partner’s interpretation of the requirements of the standard and individual preferences. Rightfully so, EQR partners feel personally invested in the engagements that they review. We have noted, however, that the challenges facing the EQR in providing a sufficiently detailed review, particularly in large multinational engagements, can be daunting. We believe such circumstances support the importance of maintaining the risk-based approach put forth by AS 7. We encourage the PCAOB to consider providing inspection observations and other guidance specifically related to executing an effective EQR process. We believe this would assist firms in developing training and guidance for EQRs that will continue to help drive consistency in approach within and across the firms.

We believe the rigor of EQR itself has considerably increased as the expectations of the overall audit has increased. As discussed further in Question 5 below, we noted more hours being dedicated by the EQR partner to fulfill his/her duties under AS 7. However, it’s important to bear in mind that audit hours in general have increased as firms continue to adopt policies and processes to improve audit quality.

*Changes in practice/Unintended consequences*

We experienced a fairly significant change in practice with the adoption of AS 7 with regard to the interaction between the lead engagement partner and EQR. Prior to AS 7, the EQR role was viewed as an “extra set of eyes” on the financial statements and often provided views and recommendations to the lead partner in addressing complex accounting matters and other audit issues, with the overall goal being the issuance of a transparent set of financial statements that are free from material misstatement. After AS 7 became effective, the focus of the EQR seemed to shift away from someone the engagement team could consult or collaborate with in deciding how to address an issue or in exploring potential approaches for a specific risk, including the proper accounting and disclosure of a transaction. With this shift in EQR focus, many engagement teams reduced communications with the EQR. We believe this was due to engagement teams seeking to avoid receiving an SED from the EQR when the engagement team had not yet reached a final conclusion or definitive course of action.

We also note that prior to AS 7, it was common for concurring partners to attend audit committee meetings and interact directly with audit committee members and management. With the adoption of AS 7, the EQR partner generally no longer interacts with the audit committee or management. While we acknowledge the importance of maintaining EQR objectivity, we believe the delay in involving the EQR until the team has concluded on a specific matter has resulted in operational challenges. The goal of issuing transparent financial statements that are free from material misstatement is still as important as having an engagement free of SEDs. However, statistics on restatements associated with engagement inspection findings suggest that while a specific audit may have had a deficiency, that deficiency was not of such magnitude to have missed a material misstatement in the financial statements. Therefore, it is important for the EQR to not lose focus on assessing how the team addressed critical accounting matters. An overemphasis on audit documentation matters may reduce the overall quality of the work and increase inefficiencies. We encourage the PCAOB to further assess this impact, as we believe firms in general have had similar experiences with the adoption of AS 7.

**Question 5: What have been the initial and recurring costs and benefits associated with the implementation of AS 7 from the perspective of auditors [only]?**

We would note that the initial costs included updating firm methodology and related tools for the AS 7 performance requirements, including the adoption, as well as concurrent training on policies related to the performance of EQRs and the identification of SEDs. While our observations are anecdotal, we believe the initial costs on these engagements have benefited audit quality, and such benefits have exceeded the initial time spent on implementing the EQR requirements. Recurring costs attributable solely to AS 7 are more difficult to isolate as the firm has instituted various additional quality measures since the standard became effective. Such measures include specific national office engagement monitoring, as well as enhanced planning meetings that include national office personnel and individual engagement audit quality monitoring, which occurs before or shortly after the auditor's report is issued. The addition of such actions along with the additional requirements set forth in AS 7 have resulted in improved audit quality as well as an increase in audit hours (in total and/or EQR-specific) for a certain population of engagements. However, it is somewhat difficult to attribute the benefits of increased audit quality to individual actions; as such, the specific benefit of AS 7 changes, while we believe them to be positive, are more anecdotal than quantifiable.

Furthermore, we believe assessing cost/benefit of implementing such standards is difficult to perform even in a controlled environment; it's even more challenging in the evolving environment of the audit profession. We are concerned that even the most thorough cost/benefit analyses will not yield definitive conclusions with regard to a standard's impact on audit quality. We also believe that any analyses would need to consider how a standard, particularly AS 7, is being interpreted by the PCAOB inspections staff during the inspection process, including issuance of comment forms and inspection reports. The observations provided by inspection staff could provide valuable information in evaluating the effectiveness of a given standard. For example, do observations noted in evaluating the compliance, or lack thereof, with AS 7 raise questions as to the intended or perceived scope of an EQR versus the expectations and needs of

regulators or stakeholders in this area? We encourage the Center for Economic Analysis to contemplate this notion as they move forward with their post-implementation review program.

**Question 6: Could AS 7 be refined or improved to better achieve its intended purpose? If so, how?**

We believe the standard provides an appropriate direction to the EQR in addressing the objectives of the review and has resulted in an overall increase in audit quality. As noted in our observations above, we believe that there are areas where further outreach, especially with regard to the EQRs interactions with the engagement team and the impact of enhanced firm monitoring actions, could result in changes that would improve the effectiveness and efficiency of the EQR process.

We believe further study is critical in maintaining the EQR process as a viable quality control function. We are concerned as to how sustainable the EQR model is as auditing and accounting continue to become more complex and financial statement users may look to expanded involvement in areas such as sustainability, non-GAAP measures, and others. We are concerned that the notion of a single person serving as EQR can be reasonably expected to fulfill all of the responsibilities in AS 7. Currently, paragraph 5 of AS 7 says, “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.” We note that the engagement partner will typically assign a team of individuals to assist in executing a quality audit. This team often includes specialists and national offices resources. As noted above, certain firms are bringing other resources to bear in evaluating and assisting with audit performance in various areas.

We think this begs the question as to whether an EQR could appropriately fulfill the requirements of AS 7 without relying, to a fairly significant extent, on the work performed by certain engagement team support. We acknowledge the note after paragraph 6 of AS 7 that allows for the use of assistants in performing the EQR as long as they “[are] independent, perform the assigned procedures with integrity and maintain objectivity in performing the review.” However, it is unclear, particularly in the context of independence and objectivity, whether the reviewer could use the work of firm-employed specialists and national office resources in performing his/her review. National office resources in particular could be viewed as independent and objective when consulting with an engagement team on a specific accounting or auditing matter. Currently, we believe utilizing national office resource to assist in the EQR process is not allowed under the standard since the national office resources could be viewed as being utilized by the engagement team for the purpose of forming the initial conclusion on a related matter and would therefore be viewed as not independent of the engagement. We encourage the Board to further consider these scenarios and circumstances in evaluating potential changes related to the use of EQR assistants and the use of specialists and national office resources.

Finally, we also encourage further consideration of the clarity of the first part of the definition of an SED regarding an engagement team failing to obtain sufficient appropriate evidence in

accordance with the standards of the PCAOB.<sup>1</sup> We believe there are various interpretations of the notion of the sufficiency of evidence that is causing difficulties and inconsistencies in practice for EQRs in determining what exactly constitutes an SED. For example, would deficiencies that result in a Part I finding in a firm's inspection report also represent an SED? Or if the findings do not relate to "significant judgments" by the engagement team, would the matter not rise to the level of saying the opinion is not supported by the audit work? We believe further clarity in evaluating the severity of the deficiencies would improve the standard.

\*\*\*\*\*

We would be pleased to discuss our comments with you. If you have any questions, please contact Trent Gazzaway, National Managing Partner of Professional Standards, at (704) 632-6834 or [Trent.Gazzaway@us.gt.com](mailto:Trent.Gazzaway@us.gt.com).

Sincerely,



---

<sup>1</sup> PCAOB AS 1220.12