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**STANDING ADVISORY GROUP MEETING**  
**DESIGNING AND IMPLEMENTING A SYSTEM OF QUALITY CONTROL**

**OCTOBER 13-14, 2010**

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**Introduction**

Public Company Accounting Oversight Board ("PCAOB" or the "Board") standards require a firm to design and implement a system of quality control to provide reasonable assurance that its personnel comply with applicable professional standards and the firm's standards of quality.<sup>1/</sup> Deficiencies identified by PCAOB inspectors in their reviews of issuer audits during the recent economic crisis suggest that improvements are needed in firms' systems of quality control.<sup>2/</sup> For example, audit deficiencies related to fair value measurements by issuers occurred despite (1) the issuance of two PCAOB

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<sup>1/</sup> Paragraph .03 of QC sec. 20, *System of Quality Control for a CPA Firm's Accounting and Auditing Practice*. References to QC sections throughout this paper are to the PCAOB's quality control standards adopted as in existence on April 16, 2003, except as superseded or amended by the PCAOB. These standards are on the PCAOB's website at: <http://www.pcaobus.org>.

<sup>2/</sup> PCAOB Release No. 2010-006, *Report on Observation of PCAOB Inspectors related to Audit Risk Areas affected by the Economic Crisis*, September 29, 2010 ("4010 Report on Economic Crisis"), available at: [http://pcaobus.org/Inspections/Documents/4010 Report Economic Crisis.pdf](http://pcaobus.org/Inspections/Documents/4010%20Report%20Economic%20Crisis.pdf).

This paper was developed by the staff of the Office of the Chief Auditor as of October 6, 2010, to foster discussion among the members of the Standing Advisory Group. It is not a statement of the Board; nor does it necessarily reflect the views of the Board or staff.

staff audit practice alerts reminding auditors of required procedures and (2) ongoing dialogue between firms and inspectors about these issues.<sup>3/</sup>

The Office of the Chief Auditor's standards-setting agenda includes a project to reconsider the Board's quality control standards.<sup>4/</sup> At the October 13-14, 2010 meeting, the Standing Advisory Group ("SAG") will discuss topics relating to the design and implementation of systems of quality control.<sup>5/</sup> Prior to that discussion, there will be a background session to give an overview of the existing quality control standards and how the Board considers audit firms' quality controls in its inspection activities.

This paper (1) provides background information regarding quality controls, (2) provides an overview of the elements of the Board's quality control standards, (3) describes considerations in designing and implementing a system of quality control, and

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<sup>3/</sup> Staff Audit Practice Alert No. 2, *Matters Related to Auditing Fair Value Measurements of Financial Instruments and the Use of Specialists* (December 10, 2007), available at: [http://pcaobus.org/Standards/QandA/12-10-2007\\_APA\\_2.pdf](http://pcaobus.org/Standards/QandA/12-10-2007_APA_2.pdf) and Staff Audit Practice Alert No. 3, *Audit Considerations in the Current Economic Environment* (December 5, 2008), available at: [http://pcaobus.org/Standards/QandA/12-05-2008\\_APA\\_3.pdf](http://pcaobus.org/Standards/QandA/12-05-2008_APA_3.pdf).

<sup>4/</sup> The PCAOB is also considering proposing rules that would require firms to make and document clear assignments of the supervision responsibilities that are already required to be part of any audit practice, without imposing any new supervision responsibilities in the Board's auditing standards and quality control standards. See PCAOB Release No. 2010-005, *Application of the "Failure to Supervise" Provision of the Sarbanes-Oxley Act of 2002 and Solicitation of Comment on Rulemaking Concepts* (August 5, 2010), available at: [http://pcaobus.org/Rules/Rulemaking/Docket031/Release\\_2010--005\\_Failure\\_to\\_Supervise.pdf](http://pcaobus.org/Rules/Rulemaking/Docket031/Release_2010--005_Failure_to_Supervise.pdf).

<sup>5/</sup> The SAG has previously discussed the existing quality control standards, including the possibility of the development of new standards on quality control. See SAG briefing papers on: "Potential Standard – Quality Control Standards" (June 21-22, 2004); "Potential Standard – Elements of Quality Control" (November 17-18, 2004); "Audit Implications of IFRS Financial Statements in US SEC Filings" (October 18, 2007); "Panel Discussion – Global Quality Control Practices" (February 27, 2008); and "Discussion – Treasury Advisory Committee's Recommendation Relating to the Feasibility of Developing Key Indicators of Audit Quality and Effectiveness" (October 22-23, 2008). Copies of these SAG briefing papers and webcast archives are available at: <http://pcaobus.org/Standards/SAG/Pages/SAGMeetingArchive.aspx>.

(4) describes potential challenges in designing and implementing a system of quality control.

## Background

The accounting profession first addressed quality control considerations for accounting firms in the 1970s in the wake of a series of accounting scandals and decisions by the U.S. Securities and Exchange Commission ("SEC") to name not only individuals in enforcement proceedings, but also auditing firms as well.<sup>6/</sup> An SEC Commissioner at that time noted that "in many cases the faults identified by the Commission [were] the results of firm insufficiencies – inadequate control, insufficient training, [and a] failure to enforce standards."<sup>7/</sup> Consequently, in December 1974, the Auditing Standards Executive Committee of the American Institute of Certified Public Accountants ("AICPA") issued Statement on Auditing Standards No. 4, *Quality Control Considerations for a Firm of Independent Auditors*. That standard recognized the need for firms to have systems of quality control and outlined the elements of a system of quality control. Subsequent quality control standards issued by the profession further explained those elements and provided additional guidance regarding the monitoring and personnel management elements, including the competencies of an audit engagement partner.

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<sup>6/</sup> See e.g., J. Michael Cook, "The Securities and Exchange Commission's First Fifty Years: An Accountant's Viewpoint," *Journal of Comparative Business and Capital Market Law* 7 (1985) pp. 361-378, available at: [http://www.law.upenn.edu/journals/jil/articles/volume7/issue3/Cook7J.Comp.Bus.&Cap.MarketL.361\(1985\).pdf](http://www.law.upenn.edu/journals/jil/articles/volume7/issue3/Cook7J.Comp.Bus.&Cap.MarketL.361(1985).pdf) and Speech by Commissioner A.A. Sommer Jr., "Accountants: A Flexible Standard," American Bar Association National Institute on Professional Liability, Montreal Canada (May 30, 1974), available at: <http://sec.gov/news/speech/1974/053074sommer.pdf>. See also Speech by Chairman Ray Garrett Jr., "Improving Financial Disclosure to Investors," AICPA (October 16, 1973), available at: <http://sec.gov/news/speech/1973/101673garrett.pdf>, which discusses the need for quality control standards.

<sup>7/</sup> See Speech by Commissioner A.A. Sommer, Jr., "The SEC and the Accounting Profession: 'Creative Tension,'" Twenty-Fifth Annual Meeting of the Northeast Regional Group of the American Accounting Association, Philadelphia, Pennsylvania (April 19, 1974), available at: <http://sec.gov/news/speech/1974/041974sommer.pdf>.

The Board's existing quality control standards include:

- QC sec. 20, *System of Quality Control for a CPA Firm's Accounting and Auditing Practice* ("QC sec. 20");
- QC sec. 30, *Monitoring a CPA Firm's Accounting and Auditing Practice* ("QC sec. 30"); and
- 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").

In addition to these standards, the Board also designated certain membership requirements of the AICPA SEC Practice Section ("SECPS") as additional quality control standards.<sup>8/</sup> The SECPS requirements adopted by the Board include:

- SECPS §1000.08(d), *Continuing Professional Education of Audit Firm Personnel*;
- SECPS §1000.08(l), *Communication by Written Statement to all Professional Personnel of Firm Policies and Procedures on the Recommendation and Approval of Accounting Principles, Present and Potential Client Relationships, and the Types of Services Provided*;
- SECPS §1000.08(m), *Notification of the Commission of Resignations and Dismissals from Audit Engagements for Commission Registrants*;
- SECPS §1000.08(n), *Audit Firm Obligations with Respect to the Policies and Procedures of Correspondent Firms and of Other Members of International Firms or International Associations of Firms*; and
- SECPS §1000.08(o), *Policies and Procedures to Comply with Independence Requirements*.

The Sarbanes-Oxley Act ("the Act") requires the Board to conduct inspections of registered firms, including the quality control systems of those firms. However, the Act requires the Board to keep quality control criticisms nonpublic unless a firm fails to

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<sup>8/</sup> These SECPS requirements are applicable only to those registered firms that were members of the SECPS on April 16, 2003.

address them to the Board's satisfaction within 12 months.<sup>9/</sup> This restriction motivates firms to undertake corrective actions. In response to successive inspections that have continued to identify audit failures, the PCAOB has pressed firms to engage in more rigorous root cause analysis and to take more significant steps to address what may be deeply rooted management and cultural impediments to audit quality.<sup>10/</sup>

The PCAOB's inspection staff routinely identifies audit deficiencies that should have been detected and remedied before the audit report was issued.<sup>11/</sup> Improvements to the design and implementation of firms' systems of quality control could have significant potential to improve audit quality by not only detecting more audit deficiencies prior to the issuance of the report, but also by preventing and deterring the occurrence of many such deficiencies.

Auditing Standard No. 7, *Engagement Quality Review*, superseded one of the SECPS requirements adopted by the Board as part of its interim quality control standards.<sup>12/</sup> Auditing Standard No. 7 requires improved engagement quality reviews,

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<sup>9/</sup> Section 104(g)(2) of the Act. The Board's process is described in PCAOB Release No. 104-2006-077, *The Process For Board Determinations Regarding Firms' Efforts to Address Quality Control Criticism in Inspection Reports* (March 21, 2006), available at: [http://pcaobus.org/Inspections/Documents/2006\\_03-21\\_Release\\_104-2006-077.pdf](http://pcaobus.org/Inspections/Documents/2006_03-21_Release_104-2006-077.pdf). A listing of firms that failed to address quality control concerns satisfactorily is available at: <http://pcaobus.org/Inspections/Reports/Pages/default.aspx>.

<sup>10/</sup> See PCAOB 2009 Annual Report available at: <http://pcaobus.org/About/Ops/Documents/Annual%20Reports/2009.pdf>. The 2009 Annual Report further states that "the PCAOB dedicated additional resources to the inspections of the largest firms in an effort to deepen its understanding of the largest firms' systems of quality control, including gaining an understanding and evaluating the specific management processes used by each firm to monitor and control the quality of their audit practices...Among other areas, the PCAOB focused on firms' ability to systematically identify, accumulate, evaluate, and respond to significant indications of weaknesses or deficiencies in audit quality on both an individual engagement level, and on a firm-wide basis."

<sup>11/</sup> See, e.g., 4010 Report on Economic Crisis.

<sup>12/</sup> Auditing Standard No. 7, *Engagement Quality Review*, superseded SECPS §1000.08(f), *Concurring Partner Review of the Audit Report and The Financial Statements of Commission Registrants*. The Board adopted Auditing Standard No. 7 in July 2009. The standard is applicable to all registered firms.

which could lead to detection of more deficiencies prior to the issuance of audit reports. Other standards-setters and regulators also have addressed improving quality controls of auditing firms.<sup>13/</sup>

## **Overview of the Elements of the Board's Quality Control Standards**

The Board's standards of quality control state that a system of quality control is broadly defined as a process to provide reasonable assurance that firm personnel comply with professional standards and the firm's standards of quality control.<sup>14/</sup> In addition, the Board's quality control standards identify five interrelated elements of quality control, which are described in the following paragraphs. The Board's quality control standards, including the SECPS requirements, further explain the elements and provide additional guidance for designing and implementing a system of quality control that encompasses those elements.

### ***Independence, Integrity, and Objectivity***

A firm should establish policies and procedures to provide the firm with reasonable assurance that personnel maintain independence (in fact and in appearance) in all required circumstances, perform all professional responsibilities with integrity, and maintain objectivity in discharging professional responsibilities.<sup>15/</sup>

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<sup>13/</sup> Certain professional organizations have recently revised their quality control standards. For example, the International Auditing and Assurance Standards Board issued International Standard on Quality Control No. 1, *Quality Controls For Firms That Perform Audits and Reviews of Financial Statements, and Other Assurance and Related Service Engagements* and International Standard on Auditing No. 220, *Quality Control For an Audit of Financial Statements*. In addition, the AICPA's Auditing Standards Board revised its existing quality control standards with the issuance of Statement on Quality Control Standards No. 7, *A Firm's System of Quality Control*. Furthermore, the UK Financial Reporting Council issued its Audit Quality Framework. The SAG previously discussed the Audit Quality Framework at its October 22-23, 2008 meeting. The briefing paper and webcast archive are available at: [http://pcaobus.org/News/Events/Pages/10222008\\_SAGMeeting.aspx](http://pcaobus.org/News/Events/Pages/10222008_SAGMeeting.aspx).

<sup>14/</sup> QC sec. 20.03.

<sup>15/</sup> QC sec. 20.09.

### ***Personnel Management***

A firm should have quality control policies and procedures that encompass hiring, assigning personnel to engagements, professional development, and advancement activities.<sup>16/</sup> Those quality control policies and procedures should provide reasonable assurance that: a) personnel hired possess the appropriate characteristics to enable them to perform competently; b) work is assigned to personnel having the degree of technical training and proficiency required in the circumstances; c) personnel participate in general and industry-specific continuing professional education and other professional development activities that enable them to fulfill responsibilities assigned and to satisfy applicable continuing professional education requirements; and d) personnel selected for advancement have the qualifications necessary for fulfillment of the responsibilities they will be called on to assume.<sup>17/</sup>

### ***Acceptance and Continuance of Clients and Engagements***

A firm should establish policies and procedures for deciding whether to accept or continue a client relationship and whether to perform a specific engagement for that client. Those policies and procedures should provide the firm with reasonable assurance that the likelihood of association with a client whose management lacks integrity is minimized.<sup>18/</sup>

### ***Engagement Performance***

A firm should establish policies and procedures to provide the firm with reasonable assurance that the work performed by engagement personnel meets applicable professional standards, regulatory requirements, and the firm's standards of quality.<sup>19/</sup> Such policies and procedures encompass all phases of the design and execution of the engagement.<sup>20/</sup> For example, a firm should establish policies and procedures to provide reasonable assurance that personnel refer to authoritative literature or other sources and consult, on a timely basis, with individuals within or

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<sup>16/</sup> QC sec. 20.12.

<sup>17/</sup> QC sec. 20.13.

<sup>18/</sup> QC sec. 20.14.

<sup>19/</sup> QC sec. 20.17.

<sup>20/</sup> QC sec. 20.18.

outside the firm when appropriate (e.g., when dealing with complex, unusual, or unfamiliar issues). Individuals consulted should have appropriate levels of knowledge, competence, judgment, and authority. The nature of the arrangements for consultation depends on a number of factors, including the size of the firm and the levels of knowledge, competence, and judgment possessed by the persons performing the work.<sup>21/</sup>

### **Monitoring**

A firm should establish policies and procedures to provide the firm with reasonable assurance that the policies and procedures established by the firm for each of the other elements of quality control are suitably designed and are being effectively applied.<sup>22/</sup> Monitoring activities consider the effects of the firm's management philosophy and the environment in which the firm practices and its clients operate and involves an ongoing consideration and evaluation of the:

- Relevance and adequacy of the firm's policies and procedures,
- Appropriateness of the firm's guidance materials and any practice aids,
- Effectiveness of professional development activities, and
- Compliance with the firm's policies and procedures.<sup>23/</sup>

The existing standards note that the nature, extent, and formality of a firm's quality control policies and procedures should be appropriately comprehensive and suitably designed in relation to the firm's size, the number of its offices, the degree of authority allowed its personnel and its offices, the knowledge and experience of its personnel, the nature and complexity of the firm's practice, and appropriate cost-benefit considerations.<sup>24/</sup> The scalability of quality control standards is important, as smaller firms may face obstacles in designing and implementing systems of quality control more suitable for larger firms (e.g., not having sufficient resources for the adequate segregation of duties).

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<sup>21/</sup> QC sec. 20.19.

<sup>22/</sup> QC sec. 30.02.

<sup>23/</sup> Ibid.

<sup>24/</sup> QC sec. 20.04.

## Considerations in Designing and Implementing a System of Quality Control

A system of quality control should be designed and implemented to prevent and deter the occurrence of audit deficiencies and detect audit deficiencies before audit reports are issued. A quality control system should: (1) appropriately develop all necessary elements, (2) integrate those elements into a complete system, and (3) emphasize an ongoing assessment and remediation of detected deficiencies.

A properly designed and implemented system of quality control can affect an individual's behavior in driving audit quality. For example:

- Policies and procedures for advancement, evaluation, and compensation should be aligned with the tone at the top set by firm's leadership that emphasizes audit quality and support good faith judgments made by individuals that may have negative consequences for client retention or profitability.
- Communicating through a written statement to all professional firm personnel the broad principles that influence the firm's quality control and operating policies and procedures may not be effective without a written annual acknowledgement by firm personnel that they have read, understood, and will comply with firm policies and procedures.

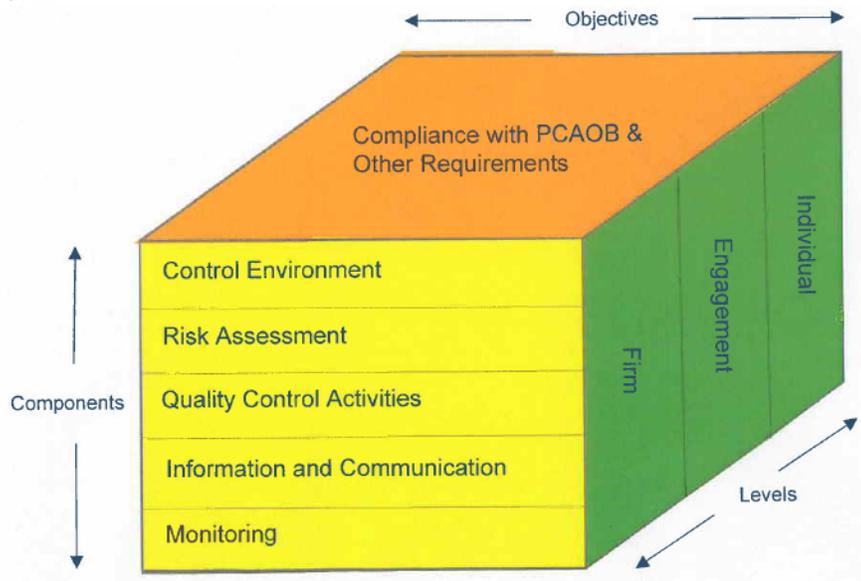
In designing and implementing a system of quality control, firms identify, assess, and address relevant risks to achieving their objectives. Risks that could negatively affect audit quality include, e.g., having excessive concerns over retaining clients or collecting fees for hours worked in excess of hours budgeted, meeting reporting deadlines even though there may be unresolved or only partially resolved audit issues, achieving revenue and profit goals as the firm's priority, addressing the increasing complexity of financial reporting, and addressing the increased requirements for applying judgment brought on by principles-based accounting standards. Risk assessment is an ongoing process that requires audit firms to identify, assess, and respond to those risks.<sup>25/</sup>

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<sup>25/</sup> Quality control experts have promoted similar approaches. For example, in his book, *Out of the Crisis*, written in 1986, W. Edwards Deming noted fourteen points for the optimization of management, including "Ceas[ing] dependence on inspection to achieve quality. Eliminate the need for inspection on a mass basis by building quality into the product in the first place." See <http://deming.org/index.cfm?content=66>.

The monitoring activities that a registered firm uses, including internal inspections, should identify and remediate the root causes of audit deficiencies. Until fully remediated, the root causes should be built into firms' risk assessment processes and communicated to all professional staff. A remediation process should be appropriately designed and implemented to provide reasonable assurance that all audit and quality control deficiencies are remediated in a timely manner.

Issuers have benefited from using an integrated framework to design and implement systems of internal control.<sup>26/</sup> An integrated framework could also be useful for designing and implementing a system of quality control. The chart below illustrates how the existing standards of quality control might be expressed as an integrated framework.<sup>27/</sup>



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<sup>26/</sup> See, e.g., *Internal Control—Integrated Framework*, published by the Committee of Sponsoring Organizations of the Treadway Commission, available at: <http://www.coso.org>.

<sup>27/</sup> The elements of quality control and other guidance in the Board's quality control standards can be expressed as components of an integrated framework. For example, the element of monitoring describes procedures consistent with the components of monitoring and risk assessment.

### Discussion Questions –

1. Could an integrated framework better emphasize the need to design and implement a system of quality control that: (1) appropriately develops all necessary elements, (2) integrates those elements of quality control into a complete system, and (3) stresses an ongoing assessment and remediation of deficiencies?
2. Would a separate risk assessment process to identify, assess, and address relevant risks to audit quality improve the design and implementation of systems of quality control?
3. What changes to the Board's quality control standards would better motivate firms to use known audit deficiencies to identify and remediate the defects in quality control that allowed the deficiencies to occur?
4. Are there lessons learned from other industries that could be useful in designing and implementing systems of quality control for accounting firms? For example, recent reforms instituted for credit rating agencies?

### Potential Challenges in Designing and Implementing a System of Quality Control

#### *Firm Culture*

During previous SAG discussions, SAG members noted that a firm's culture is important in establishing an effective system of quality control.<sup>28/</sup> Some SAG members also noted the benefits of certain internal controls adopted by public companies (e.g., whistleblower hotline and a formal code of conduct).

The culture of an audit firm is affected by the firms' business objectives that could compete with the objective to produce high quality audits. The quality of a firm's work depends on, among other things, the motivation and competence of personnel to perform, supervise, and review the work.<sup>29/</sup> A firm's quality control policies and procedures should provide the firm with reasonable assurance that its personnel maintain independence in all required circumstances, perform all professional

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<sup>28/</sup> See webcast archives for the SAG discussions: "Potential Standard – Quality Control Standards" (June 21-22, 2004); "Potential Standard – Elements of Quality Control" (November 17-18, 2004), available at: <http://pcaobus.org/Standards/SAG/Pages/SAGMeetingArchive.aspx>.

<sup>29/</sup> QC sec. 20.12.

responsibilities with integrity, and maintain objectivity in discharging professional responsibilities.<sup>30/</sup>

### ***Changes in Financial Reporting Frameworks***

The movement to principles-based accounting standards could impact the exercise of judgment by auditors and could require changes in the policies and procedures regarding consultation.<sup>31/</sup> A consistent approach to recurring accounting issues across a firm and a global audit network could require increased level of consultation with individuals with appropriate levels of knowledge, competence, judgment, and authority regarding complex, unusual, or unfamiliar issues. Many accounting firms use a national office to respond to such issues.

### ***Cross-Border Auditing***

Many domestic issuers have branches, subsidiaries, and joint ventures around the world that contribute to those companies' operating results and financial position. Global audit networks were developed, in part, to audit these multi-national corporations.<sup>32/</sup> Registered public accounting firms with U.S.-based multi-national audit clients often use the work of other network firms to assist in audits of non-U.S. operations, i.e., referred work.<sup>33/</sup> Involving another firm in an audit can present

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<sup>30/</sup> QC sec. 20.09.

<sup>31/</sup> For additional discussion regarding how changes in accounting standards could impact the exercise of judgment, see e.g., *Study Pursuant to Section 108(d) of the Sarbanes-Oxley Act of 2002 on the Adoption by the United States Financial Reporting System of a Principles-Based Accounting System*, available at: <http://sec.gov/news/studies/principlesbasedstand.htm>; July 2004 *FASB Response to SEC Study on the Adoption of a Principles-Based Accounting System*, available at: [http://www.fasb.org/response\\_sec\\_study\\_july2004.pdf](http://www.fasb.org/response_sec_study_july2004.pdf); and the final report of the SEC's Advisory Committee on Improvements to Financial Reporting, available at: <http://www.sec.gov/about/offices/oca/acifr/acifr-finalreport.pdf>.

<sup>32/</sup> See U.S. Government Accountability Office Report to the Senate Banking Committee on Banking, Housing and Urban Affairs and the House Committee on Financial Services, *Public Accounting Firms Mandated Study on Consolidation and Competition* (July 2003), available at: <http://www.gao.gov/new.items/d03864.pdf>.

<sup>33/</sup> AU sec. 543, *Part of Audit Performed by Other Independent Auditors*, ("AU sec. 543") provides requirements for auditors using the work and reports of another auditor. The Office of the Chief Auditor has a standards-setting project regarding AU

challenges, e.g., cultural differences, different regulatory environments, and language barriers.<sup>34/</sup> The Board's quality control standards state that the system of quality control should provide the firm with reasonable assurance that the segments of the firm's engagements performed by its foreign offices or by its domestic or foreign affiliates or correspondents are performed in accordance with PCAOB standards.<sup>35/</sup>

PCAOB inspectors have identified deficiencies associated with the use of firms in a global audit network. For example, inspectors have noted the lack of sufficient communications with affiliates, the failure to identify audit deficiencies in the work of an affiliate, and the failure to appropriately resolve errors identified by an affiliated firm. In addition, the Board's inspection teams noted instances in which firms failed to provide their engagement partners with all relevant internal inspection information available to the firm about the foreign-affiliate firms and personnel whose work those partners use in their audits and where the U.S. partners did not inquire about the results of the internal inspections of the firms and partners responsible for auditing the foreign operations of their U.S. issuers.<sup>36/</sup>

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sec. 543 on its agenda. The SAG discussed this topic at its April 7-8, 2010 meeting. The webcast archive and briefing paper are available at: [http://pcaobus.org/News/Events/Pages/04072010\\_SAGMeeting.aspx](http://pcaobus.org/News/Events/Pages/04072010_SAGMeeting.aspx). See also Practice Alert No. 6: *Auditor Considerations Regarding Using the Work of Other Auditors and Engaging Assistants from Outside the Firm* (July 12, 2010), [http://pcaobus.org/Standards/QandA/2010-07-12\\_APA\\_6.pdf](http://pcaobus.org/Standards/QandA/2010-07-12_APA_6.pdf), which discusses observations from the Board's inspection process which suggest that some firms may not be complying with AU sec. 543.

<sup>34/</sup> The large accounting firms often refer to their affiliation of firms domiciled in various countries as global audit networks. Global audit networks present themselves, through their marketing and branding efforts, as global firms that deliver seamless audit products across international boundaries. However, global audit networks are structured legally as networks of firms, rather than as a single global firm.

<sup>35/</sup> QC sec. 20.06.

<sup>36/</sup> PCAOB Release No. 2008-008, *Report on the PCAOB's 2004, 2005, 2006, and 2007 Inspection of Domestic Annually Inspected Firms* (December 5, 2008).

**Discussion Questions –**

5. What changes to the Board's quality control standards might be necessary in light of the potential challenges to designing and implementing a system of quality control? Are there other challenges that should be considered?
6. What attributes are necessary for a firm culture to be conducive to audit quality? What requirements or other measures could the PCAOB propose to motivate firms to promote a firm culture that minimizes incentives that do not promote audit quality?
7. What quality controls should be in place when using the work of a foreign affiliated firm?

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The PCAOB is a private-sector, non-profit corporation, created by the Sarbanes-Oxley Act of 2002, to oversee the auditors of public companies in order to protect the interests of investors and further the public interest in the preparation of informative, fair, and independent audit reports.