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Sarbanes-Oxley Act of 2002 (the "Act") expressly directs the Board to establish auditing standards that require registered public accounting firms to prepare and maintain, for at least seven years, audit documentation "in sufficient detail to support the conclusions reached" in the auditor's report. Audit documentation is one of only a few topics that the Act expressly requires the Board to address in its standards. Accordingly, the Board has made audit documentation a priority.

The Board's standard on audit documentation will be one of the fundamental building blocks on which both the integrity of audits and the Board's oversight will rest. The integrity of the audit depends in large part on the existence of a complete and understandable record of the work that the auditor performed, of the conclusions that the auditor reached, and of the evidence that supports those conclusions. Meaningful review by a second partner, or by the Board in the context of its inspections, would be difficult or impossible without adequate documentation. Clear and comprehensive audit documentation is essential in order to enhance the quality of the audit and for the Board to fulfill its mandate to inspect registered public accounting firms "to assess the degree of compliance" of those firms with applicable standards and laws.

Appendices 1 and 2 to this release contain, respectively, the text of the proposed auditing standard, *Audit Documentation*, and the proposed amendment to AU Section 543. Section A of this release provides an overview of the proposed new standard and the proposed amendment. Section B of this release discusses the proposed implementation date and Section C requests comments and describes how they may be submitted to the Board.

### **A. Audit Documentation**

Auditors support the conclusions in their reports with a work product commonly referred to as work papers or audit documentation. Audit documentation is the principal record of the basis for the conclusions in the auditor's report. Audit documentation also facilitates the planning, performance, and supervision of the engagement and provides the basis for the review of the quality of the work by providing the reviewer with written documentation of the evidence supporting the auditor's significant conclusions. Examples of audit documentation include memoranda, correspondence, and schedules. Audit documentation may be in the form of paper, electronic files, or other media.

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Section 103 of the Act specifically directs the Board to "include[,] in the auditing standards that it adopts, requirements that each registered public accounting firm shall . . . prepare, and maintain . . . , audit work papers, and other information related to any audit report, in sufficient detail to support the conclusions reached" in an audit report of a public company.<sup>2/</sup> In response to this mandate, the Board commenced a standards-development project on audit documentation by convening a public roundtable discussion on September 29, 2003 to discuss issues and hear views on audit documentation. Before that roundtable discussion, the Board prepared and released a briefing paper on audit documentation, which posed several questions to identify the objectives – and the appropriate scope and form – of audit documentation.<sup>3/</sup> In addition, the Board asked participants to address specific issues in practice relating to, among other things, changes in audit documentation after an audit report has been released, essential elements and the appropriate amount of detail of audit documentation, the effect on audit documentation of a principal auditor's decision to use the work of other auditors, and retention of audit documentation.

The comments the Board received at this roundtable discussion played a significant role in its development of its proposed standard on audit documentation and proposed amendment to its interim auditing standard. Based on these comments, and in order to implement Section 103(a)(2)(A)(i) of the Act, the Board has proposed certain changes to the existing requirements, principally described in the American Institute of Certified Public Accountant's Statement on Auditing Standards ("SAS") No. 96. The more significant differences between existing requirements and these proposals on audit documentation are as follows –

**Reviewability Standard.** This proposed standard would adopt the substance of the General Accounting Offices' ("GAO") documentation standard for government and other audits conducted according to *generally accepted government auditing standards* ("GAGAS"), which requires that "audit documentation related to planning, conducting, and reporting on the audit should contain sufficient information to enable an experienced auditor who has had no previous connection with the audit to ascertain

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<sup>2/</sup> See Sarbanes-Oxley Act, Section 103(a)(2)(A).

<sup>3/</sup> See Briefing Paper for the Roundtable on Audit Documentation, dated September 10, 2003. The transcript of the September 29 roundtable discussion, and copies of the briefing paper, are available on the Board's Web site.

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from the audit documentation the evidence that supports the auditors' significant judgments and conclusions." Field Work Standards for Financial Audits, Government Auditing Standards § 4.22 (U.S. Government Accounting Office, 2003 rev.). This has been an important requirement in the field of government auditing because government audits have long been reviewed by GAO auditors who, although experienced in auditing, do not participate in the actual audits. Public company audits will now, under the Act, be subject to review by PCAOB inspectors, and therefore a documentation standard that would enable such an inspector to understand the work that was performed in the audit seems appropriate.

Specifically, the Board's proposed standard would require that audit documentation contain sufficient information to enable an *experienced auditor, having no previous connection with the engagement*, to understand the work that was performed, who performed it, when it was completed, and the conclusions reached. This experienced auditor also must be able to determine who reviewed the work and the date of such review.

**Rebuttable Presumption.** In order to improve the completeness and reliability of written documentation, the proposed standard would adopt the substance of the state of California's statute on audit documentation, which creates a rebuttable presumption that the failure to document work performed indicates that the work was not performed. See California Business and Professions Code § 5097(c) (Deering 2003). Under the proposal, the failure to document in the work papers that an audit procedure was performed, that evidence was obtained, or that a conclusion was reached would create a presumption that such procedure was not performed, that the evidence was not obtained, or that the conclusion was not supported. The proposed presumption could be rebutted by persuasive evidence that the procedures were applied, the evidence was obtained, or sufficient support was provided for the conclusions reached. The Board contemplates that oral explanation alone would not constitute persuasive other evidence and invites comment on the addition of such a requirement to the proposed standard.

**Retention of Audit Documentation.** The proposed standard would require that an auditor retain audit documentation for seven years after completion of the engagement, which is the minimum period permitted under Section 103(a) of the Act. In addition, the proposed standard would add a new requirement that the audit documentation must be assembled for retention within a reasonable period of time after

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the auditor's report is released. Such reasonable period of time ordinarily should not exceed 45 days. During the roundtable discussion on September 29, 2003, there was a general agreement that the auditor should be allowed a reasonable period of time to assemble the working papers after the release of the auditor's report.

**Subsequent Changes to Audit Documentation.** The proposed standard would also require that any changes to the working papers after completion of the engagement be documented without deleting or discarding the original documents. Such documentation must indicate the date the information was added, by whom it was added, and the reason for adding it.

**Multi-location Audits.** The proposed standard would require that sufficient audit documentation, including documentation of work performed by others, be retained by the office issuing the auditor's report. With respect to the audit documentation related to the work performed by others, the auditor issuing the report ordinarily should retain the original audit documentation or copies of such documentation. The auditor issuing the report may, however, prepare and retain audit documentation of the work performed by others as a part of the review of such work, as long as this documentation complies with the requirements of this proposed standard. This provision of the proposed standard is based on the comments of several participants at the September 29, 2003 roundtable discussion, who raised the issue that working papers from the audits of foreign affiliates should be available and accessible at the accounting firm's office issuing the audit report. This requirement would improve audit quality by enhancing the probability that *all* audit documentation will be prepared consistently with the same standards of audit quality.

**Using the Work of Other Auditors.** When reporting on a company's consolidated financial statements, an auditor may use the work of other auditors who have audited one or more affiliates or divisions of the company. When more than one auditor is involved in an audit engagement, one of the firms typically serves as the principal auditor. If a firm decides to serve as the principal auditor, then the firm must decide whether to make reference in the auditor's report to the audit performed by the other auditor. If the principal auditor decides to assume responsibility for the work of other auditors, then the principal auditor will not make reference to the work of other auditors in his or her audit report. However, if the principal auditor decides not to assume that responsibility, then the principal auditor should clearly indicate the division

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of responsibility between the principal auditor and other auditors in expressing an opinion on the consolidated financial statements.

In connection with the proposed requirement for the issuing office to retain all audit documentation, the proposed amendment to the interim auditing standard, AU Section 543, would help to ensure that proper audit documentation is prepared and retained when a principal auditor *decides not to make reference* to the work of other auditors and the principal auditor performs an adequate review of the audit documentation prepared by the other auditor.

### **B. Implementation Date of the Proposed Standard and Related Amendment**

The Board is proposing June 15, 2004 as the implementation date for its standard, *Audit Documentation*, and related amendment to AU Section 543. Although, early implementation of the standard and related amendment would be permitted, the standard and amendment would be mandatory for engagements completed on or after June 15, 2004. The Board is also requesting comment on this proposed implementation date.

### **C. Opportunity for Public Comment**

The Board will seek comment on the proposed standard and amendment for a 60-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 may also be submitted by e-mail to [comments@pcaobus.org](mailto:comments@pcaobus.org) or through the Board's Web site at [www.pcaobus.org](http://www.pcaobus.org). All comments should refer to PCAOB Rulemaking Docket Matter No. 012 in the subject or reference line and should be received by the Board no later than 5:00 p.m. EST on January 20, 2004.

The Board will carefully consider all comments received. Following the close of the comment period, the Board will determine whether to adopt a final standard and amendment, with or without amendments. Any final standard and amendment adopted will be submitted to the Securities and Exchange Commission 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 deemed to be rules under the Act.

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On the 21st day of November, in the year 2003, 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  
Acting Secretary

November 21, 2003

APPENDICES –

1. *Proposed Auditing Standard – Audit Documentation*
2. *Proposed Amendment to Interim Auditing Standards – Part of Audit Performed by Other Independent Auditors*

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**APPENDIX 1 – PROPOSED AUDITING STANDARD – AUDIT DOCUMENTATION**

**AUDITING AND RELATED PROFESSIONAL PRACTICE STANDARDS**

*Proposed Auditing Standard—*

***AUDIT DOCUMENTATION***



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### STATEMENT OF AUTHORITY

The Public Company Accounting Oversight Board (the "Board") is a private-sector, non-profit corporation created by the Sarbanes-Oxley Act of 2002 (the "Act") 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.

The Board has adopted Rule 3100 to require all registered public accounting firms to adhere to the Board's auditing and related professional practice standards (including interim professional standards) in the audits of public companies. Any registered public accounting firm that fails to adhere to the Board's standards is subject to disciplinary proceedings in accordance with Section 105 of the Act and the Board's rules.

Reference in the Board's standards to "the auditor" means a registered public accounting firm or an associated person of such a firm as defined in the Act and the Board's rules, unless specifically stated otherwise.

Reference in the Board's standards to the AICPA Professional Standards refers to those professional standards as they existed on April 16, 2003, the date the Board adopted them as interim standards.

The Board has proposed Rule 3101 regarding the use of certain terms in the Board's standards.<sup>2/</sup> The Board's standards use the words "must," "shall," and "is required" to indicate unconditional obligations. The auditor must accomplish obligations of this type in all cases in which the circumstances exist to which the obligation applies. The auditor's performance of these obligations is necessary to the accomplishment of the audit. The standards use the word "should" to indicate obligations that are presumptively mandatory. The auditor must comply with the requirements of this nature specified in the Board's standards unless the auditor can demonstrate, by verifiable objective and documented evidence, that alternative actions he or she followed in the circumstances were sufficient to achieve the objectives of the standard and serve adequately to protect the interests of investors and further the preparation of informative, fair, and independent audit reports. The Board uses the words "may," "might," "could," or other terms and phrases to describe actions and procedures that auditors have a professional obligation to consider. Matters described in this fashion

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<sup>2/</sup> See PCAOB Release No. 2003-018, *Proposed Rule Regarding Certain Terms Used in Auditing and Related Professional Practice Standards*.

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require the auditor's attention and understanding. How and whether the auditor implements these matters in an audit will depend on the exercise of professional judgment in the circumstances. Additionally, appendices to the Board's standards are an integral part of the standard and carry the same authoritative weight as the body of the standard.

This Statement of Authority is an integral part of the Board's auditing and related professional practice standards.

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### **Auditing and Related Professional Practice Standards**

#### **Proposed Auditing Standard**

##### ***Audit Documentation***

**[supersedes AU sec. 339]**

## **Introduction**

1. This standard establishes general requirements for documentation the auditor should prepare and retain in connection with any engagement conducted in accordance with auditing and related professional practice standards. This standard does not supplant specific documentation requirements of other auditing and related professional practice standards.

### **Objectives of Audit Documentation**

2. *Audit documentation* is the principal record of the basis for the auditor's conclusions and provides the principal support for the representations in the auditor's report. Audit documentation also facilitates the planning, performance, and supervision of the engagement and provides the basis for the review of the quality of the work by providing the reviewer with written documentation of the evidence supporting the auditor's significant conclusions. Audit documentation includes records on the planning and performance of the work, the procedures performed, evidence obtained, and conclusions reached by the auditor. Audit documentation also may be referred to as *work papers* or *working papers*.

3. Audit documentation is reviewed by members of the engagement team performing the work and by others. For example:

- a. Auditors who are new to an engagement review the prior year's documentation to understand the work performed as an aid in planning and performing the current engagement.
- b. Supervisory personnel review documentation prepared by assistants on the engagement.

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- c. Engagement partners and engagement quality control reviewers review documentation to understand how the engagement team reached significant conclusions and whether there is adequate evidential support for those conclusions.
- d. A successor auditor reviews a predecessor auditor's audit documentation.
- e. Internal and external inspection teams review documentation to assess audit quality and compliance with auditing and related professional practice standards; applicable laws, rules, and regulations; and the firm's own quality control policies.
- f. Others, including advisors engaged by the audit committee or representatives of a party to an acquisition might review audit documentation.

## **Content of Audit Documentation**

- 4. The auditor must prepare audit documentation in connection with each engagement conducted in accordance with auditing and related professional practice standards. Audit documentation ordinarily consists of memoranda, correspondence, schedules, and other documents created or obtained in connection with the engagement and may be in the form of paper, electronic files, or other media.
- 5. Audit documentation 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 procedures performed, evidence obtained, and conclusions reached, and
  - b. To determine who performed the work and the date such work was completed as well as the person who reviewed the work and the date of such review.
- 6. Auditors, including any specialists, should document the procedures performed, evidence obtained, and conclusions reached. Failure to do so creates a presumption

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that the procedures were not applied, the evidence was not obtained, and the conclusions reached were not suitably supported. This presumption is rebuttable by persuasive other evidence that the procedures were applied and the evidence was obtained to provide sufficient support for the conclusions reached.

7. Because audit documentation provides the principal support for the representations in the auditor's report, it should:

- a. Demonstrate how the audit complied with auditing and related professional practice standards;
- b. Support the basis for the auditor's conclusions concerning every material financial statement assertion; and
- c. Demonstrate that the underlying accounting records agreed or reconciled with the financial statements.

8. Certain matters, such as auditor independence and staff training and proficiency, may be documented in a central repository for the firm or the particular office participating in the engagement. If such matters are documented in a central repository, the audit documentation of the engagement should contain a reference to the central repository. Documentation of matters unique to a particular engagement should be included in the audit documentation of the pertinent engagement.

9. The auditor must document significant findings or issues, actions taken to address them (including additional evidence obtained), and the basis for the conclusions reached. *Significant findings or issues* include, but are not limited to, the following:

- a. Significant matters involving the selection, application, and consistency of accounting principles, including related disclosures. Such significant matters include accounting for complex or unusual transactions, accounting estimates, and uncertainties as well as related management assumptions.
- b. Results of auditing procedures that indicate a need for significant modification of planned auditing procedures or the existence of material

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misstatements or omissions in the financial statements or the existence of significant deficiencies in internal control over financial reporting.

- c. Audit adjustments and the ultimate resolution of these items. For purposes of this standard, an *audit adjustment* is a proposed correction of a misstatement of the financial statements that could, in the auditor's judgment, either individually or in the aggregate, have a material effect<sup>1/</sup> on the company's financial reporting process. Audit adjustments include corrections of misstatements, of which the auditor is aware, that were or should have been proposed based on the known audit evidence.
- d. Disagreements among members of the engagement team or with others consulted on the engagement about conclusions reached on significant accounting or auditing matters.
- e. Significant findings or issues identified during the review of quarterly financial information.
- f. Circumstances that cause significant difficulty in applying auditing procedures.
- g. Significant changes in the assessed level of audit risk for particular audit areas and the auditor's response to those changes.
- h. Any other matters that could result in modification of the auditor's report.

10. The auditor must identify all significant findings or issues in an engagement completion memorandum. This memorandum should be as specific as necessary in the circumstances for a reviewer to gain a thorough understanding of the significant findings or issues. This memorandum should include cross-references, as appropriate, to other supporting audit documentation.

11. Documentation of auditing procedures that involve the inspection of documents or confirmation, such as tests of details and tests of operating effectiveness of controls,

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<sup>1/</sup> Materiality includes both quantitative and qualitative considerations as discussed in SEC Staff Accounting Bulletin No. 99.

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should include identification of the items tested.<sup>2</sup> Documentation of auditing procedures that involve the inspection of significant contracts or agreements should include abstracts or copies of the documents.

12. In addition to the documentation necessary to support the auditor's final conclusions, information the auditor has identified relating to significant findings or issues that is inconsistent with or contradicts the auditor's final conclusions must also be included in the audit documentation. The relevant records to be retained include, but are not limited to, procedures performed in response to the information, and records documenting consultations on, or resolutions of, differences in professional judgment among members of the audit team or between the audit team and others consulted.

### Retention of and Subsequent Changes to Audit Documentation

13. Audit documentation must be retained for seven years from the date of completion of the engagement, as indicated by the date of the auditor's report,<sup>3</sup> unless a longer period of time is required by law.

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<sup>2/</sup> The identification of the items tested may be satisfied by indicating the source from which the items were selected and the specific selection criteria, for example:

- If an audit sample is selected from a population of documents, the documentation should include identifying characteristics (for example, the specific check numbers of the items included in the sample).
- If all items over a specific dollar amount are selected from a population of documents, the documentation need describe only the scope and the identification of the population (for example, all checks over \$10,000 from the October disbursements journal).
- If a systematic sample is selected from a population of documents, the documentation need only provide an identification of the source of the documents and an indication of the starting point and the sampling interval (for example, a systematic sample of sales invoices was selected from the sales journal for the period from October 1 to December 31, starting with invoice number 452 and selecting every 40<sup>th</sup> invoice).

<sup>3/</sup> If a report is not issued in connection with an engagement, then the date of completion of the engagement would be the date that fieldwork was substantially completed.

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14. Prior to granting permission to use the auditor's report in connection with the issuance of the company's financial statements, the auditor must have completed all necessary auditing procedures and obtained sufficient evidence to support the representations in the auditor's report. A complete and final set of audit documentation must be assembled for retention within a reasonable period of time following the first time the auditor grants permission to use the auditor's report in connection with the issuance of the company's financial statements. Such reasonable period of time ordinarily should not be more than 45 days.

15. Circumstances may require subsequent additions to the audit documentation. If evidence is obtained after completion of the engagement, or if work performed before engagement completion is documented after completion, the documentation added must indicate the date the information was added, by whom it was added, and the reason for adding it. Audit documentation must not be deleted or discarded; however, information may be added, including an explanation of its relevance, as long as the information identifies the date the information was added; by whom it was added; and the reason for adding it. The auditor should also identify and document changes to audit documentation as a result of post-issuance procedures. Documentation should include the nature of the change, the date of such change, by whom the change was made, and the reason for the change.

16. Audit documentation sufficient to meet the requirements of paragraphs 4-12 (including documentation of work performed by others, such as affiliated firms) must be retained by the office issuing the auditor's report. With respect to the audit documentation related to the work performed by others, the auditor issuing the report ordinarily should retain the original audit documentation or copies of such documentation. Alternatively, if the auditor considers it necessary in the circumstances, the auditor issuing the report should prepare and retain audit documentation of the work performed by others as a part of the review required by paragraph 12 of AU sec. 543, *Part of Audit Performed by Other Independent Auditors*, as long as the audit documentation complies with paragraphs 4-12 of this standard.



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17. The auditor also may be required to maintain documentation in addition to that required by this standard.<sup>4/</sup>

### **Implementation Date**

18. This standard will apply to engagements completed on or after June 15, 2004.

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<sup>4/</sup> For example, the SEC requires auditors to retain memoranda, correspondence, communications (for example, electronic mail), other documents, and records (in the form of paper, electronic, or other media) that are created, sent, or received in connection with an engagement conducted in accordance with auditing and related professional practice standards and that contain conclusions, opinions, analyses, or data related to the engagement. (Retention of Audit and Review Records, 17 CFR § 210.2-06, effective for audits or reviews completed on or after October 31, 2003.)

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**APPENDIX 2 – PROPOSED AMENDMENT TO INTERIM AUDITING STANDARDS – PART OF AUDIT  
PERFORMED BY OTHER INDEPENDENT AUDITORS**

**AUDITING AND RELATED PROFESSIONAL PRACTICE STANDARDS**

*Proposed Amendment to Interim Auditing Standards—*

***PART OF AUDIT PERFORMED BY OTHER INDEPENDENT  
AUDITORS***

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### **Part of Audit Performed by Other Independent Auditors – An Amendment to Interim Standards**

In reporting on a company's consolidated financial statements, an auditor may use the work of other auditors who have audited one or more affiliates or divisions of the company. When more than one auditor is involved in an audit engagement, one of the firms typically serves as the principal auditor. In considering whether a firm may serve as the principal auditor, the firm considers, among other things, the materiality of the portion of the financial statements the firm audited in relation to the consolidated group as well as the materiality of the other components audited by other firms.

If the firm decides to serve as the principal auditor, then the firm must decide whether to make reference in the auditor's report to the audit performed by the other auditor. If the principal auditor decides to assume responsibility for the work of other auditors, then the principal auditor will not make reference to the work of other auditors in his or her audit report. However, if the principal auditor decides not to assume that responsibility, then the principal auditor should indicate clearly the division of responsibility between the principal auditor and other auditors in expressing an opinion on the consolidated financial statements. Existing guidance when using the work of other auditors is contained in AU sec. 543, *Part of Audit Performed by Other Independent Auditors*. However, this existing standard does not establish any specific documentation requirements.

This proposed amendment (below) is considered necessary to ensure that proper audit documentation is prepared and retained when a principal auditor *decides not to make reference* to the work of other auditors. This proposed amendment is not the result of a comprehensive review of existing standards, which will take place at a future date.

#### **This proposal would amend AU sec. 543.12 as follows:**

When the principal auditor decides not to make reference to the audit of the other auditor, in addition to satisfying himself as to the matters described in AU sec. 543.10, the principal auditor should review the audit documentation of the other auditor to the same extent and in the same manner that the audit work of all those who participated in the engagement is reviewed. Sufficient audit documentation of the work performed by the other auditor should be incorporated in the audit documentation of the principal auditor to meet all the requirements of PCAOB Auditing and Related Professional Practice Standards No. X, as if the

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principal auditor had performed the work himself or herself. In addition to reviewing the audit documentation of the other auditor, the principal auditor should consider whether it is necessary to visit the other auditor and discuss the audit procedures followed and the results thereof and whether it is necessary to instruct the other auditor as to the scope of work to be performed.