PCAOB
PUBLIC COMPANY ACCOUNTING OVERSIGHT BOARD

# General Responsibilities of the Auditor in Conducting an Audit and Amendments to PCAOB Standards

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PCAOB Rulemaking
Docket Matter No. 049

Summary: The Public Company Accounting Oversight Board ("PCAOB" or the "Board") is adopting a new auditing standard, AS 1000, *General Responsibilities of the Auditor in Conducting an Audit*, and amending other related PCAOB standards. The new auditing standard addresses the general responsibilities of the auditor, such as due professional care and professional skepticism, when conducting an audit in accordance with the standards of the PCAOB.

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Amendments:

The Board is adopting amendments to its standards that:

(1) Adopt AS 1000, *General Responsibilities of the Auditor in Conducting an Audit*;

(2) Rescind:
- AS 1001, *Responsibilities and Functions of the Independent Auditor*;
- AS 1005, *Independence*;
- AS 1010, *Training and Proficiency of the Independent Auditor*;
- AS 1015, *Due Professional Care in the Performance of Work*; and
- AS 2815, *The Meaning of "Present Fairly in Conformity with Generally Accepted Accounting Principles"*;

(3) Revise:
- AS 1201, *Supervision of the Audit Engagement*;
- AS 1215, *Audit Documentation*;
- AS 2101, *Audit Planning*; and
- AS 2810, *Evaluating Audit Results*; and

(4) Make additional conforming amendments to PCAOB standards.

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# I. EXECUTIVE SUMMARY

We are adopting a new auditing standard, AS 1000, *General Responsibilities of the Auditor in Conducting an Audit* ("new standard," "final standard," or "AS 1000"). The new standard replaces a group of standards originally developed by the American Institute of Certified Public Accountants ("AICPA") and adopted on an interim basis by the PCAOB in 2003. That group of standards established the general principles and responsibilities of the auditor when conducting an audit ("foundational standards"). The general principles and responsibilities addressed by the foundational standards include reasonable assurance, due professional care, professional skepticism, independence, competence, and professional judgment. These principles and related responsibilities provide a foundation for the proper performance of the audit.

Through this standard-setting project, we have reaffirmed the general principles and responsibilities of the auditor so that the foundation underlying our standards continues to be sound and appropriate for performing high-quality audits. These principles and responsibilities, enhanced and consolidated into a single auditing standard, together with related amendments, will modernize the auditing standards to better address fundamental aspects of the audit and provide auditors with better direction to protect investors and further the public interest in the preparation of informative, accurate, and independent auditor's reports.

AS 1000 will replace four standards that set forth the general principles and responsibilities of the auditor: AS 1001, *Responsibilities and Functions of the Independent Auditor*; AS 1005, *Independence*; AS 1010, *Training and Proficiency of the Independent Auditor*; and AS 1015, *Due Professional Care in the Performance of Work*. AS 1000 combines and updates the general principles and responsibilities of these standards to reflect developments in the auditing environment.

We are also amending certain other PCAOB standards that address responsibilities fundamental to the conduct of an audit. These amendments clarify the engagement partner's responsibility to exercise due professional care related to supervision and review of the audit, accelerate the documentation completion date by reducing the maximum period for the auditor to assemble a complete and final set of audit documentation from 45 days to 14 days, and clarify the auditor's responsibility to evaluate whether the financial statements are "presented fairly." Finally, we are adopting additional amendments to conform to these changes.

After carefully considering the comments we received, we are adopting the amendments substantially as proposed, with revisions that reflect the input of commenters.

**Reasons for and Key Provisions of the New Standard and Amendments**

Since the PCAOB's adoption of the foundational standards in 2003, the auditing environment has evolved, including:

- Changes to auditing requirements through Board-issued standards;
- New or revised independence requirements issued by the Board; and
- Advancements in technology that are increasing the availability of electronic audit tools and use of audit software.

The new standard and related amendments we are adopting will modernize PCAOB standards to:

- Reflect changes in the auditing environment;
- Eliminate outdated and inconsistent language; and
- Achieve consistency with Board-issued standards.

AS 1000 and the related amendments modernize, clarify, and streamline the general principles and responsibilities of the auditor and provide a more logical presentation, which should enhance the useability of the standards by making them easier to read, understand, and apply.

We are clarifying the auditor's responsibility to evaluate whether the financial statements are "presented fairly." We are also clarifying the engagement partner's due professional care responsibilities by adding specificity to certain audit performance principles set out in the standards. Finally, the accelerated documentation completion date reflects changes in the auditing environment, including advancements in technology that have enabled auditors to assemble a complete and final set of audit documentation in less time than in a paper-based environment. The new documentation completion date reduces the window of opportunity for improper alteration of audit documentation and also enables the Board to potentially begin the inspection process sooner after completion of an audit, which we believe can enhance the Board's efforts to improve audit quality and promote investor protection, ultimately enhancing investor confidence.

The new standard and related amendments will apply to all audits conducted under PCAOB standards. Subject to approval by the U.S. Securities and Exchange Commission ("SEC" or "Commission"), the new standard and related amendments will take effect for audits of financial statements for fiscal years beginning on or after December 15, 2024, except that, for registered public accounting firms ("firms") that provide audit opinions for 100 or fewer issuers (i.e., smaller firms), the amendment relating to the documentation completion date will take effect for audits of financial statements for fiscal years beginning on or after December 15, 2025. More information on the effective dates is discussed in Section VI of this release.

This release provides background on the Board's standard-setting project, discusses the new standard and related amendments, and includes an economic analysis that further

explains the need for standard setting and the anticipated economic impacts of the changes. This release also includes three appendices. Appendix 1 sets forth the text of the new standard, Appendix 2 key amendments to related PCAOB auditing standards, and Appendix 3 conforming amendments to other PCAOB standards.

## II. BACKGROUND

In April 2003, the Board adopted, on an interim basis, the generally accepted auditing standards of the AICPA's Auditing Standards Board ("interim standards") and the related auditing interpretations as they existed then.[1] At that time, the Board stated that it would determine whether the interim standards "should become permanent standards of the Board, should be repealed, or should be modified."[2] Since then, the Board has adopted a number of new auditing standards that supersede or amend portions of the interim standards and related auditing interpretations.[3] However, certain remaining interim standards, including those that address the general principles and responsibilities of the auditor, have continued to be in effect substantially in the form adopted.

Since the adoption of the interim standards, the auditing environment has evolved in many ways, including (i) changes to auditing requirements through Board-issued standards; (ii) new or revised independence requirements issued by the Board;[4] and (iii) advancements in technology that are increasing the availability of electronic audit tools and the use of audit software. While these developments have generally been reflected through amendments to some interim standards and related interpretations in connection with the Board's standard-setting initiatives, the 2022-2026 Strategic Plan reinforced our intent "to modernize and streamline our existing standards and to issue new standards where necessary to meet today's needs" as part of the PCAOB's investor protection mission.[5]

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[1] *See Establishment of Interim Professional Auditing Standards*, PCAOB Rel. No. 2003-006 (Apr. 18, 2003). The auditing interpretations were the publications entitled "Auditing Interpretations" issued by the AICPA Auditing Standards Board, as they existed and were effective as of April 2003.

[2] *See* PCAOB Rel. No. 2003-006.

[3] *See, e.g.*, AS 1201, *Supervision of the Audit Engagement*; AS 1215, *Audit Documentation*; AS 2101, *Audit Planning*; AS 2810, *Evaluating Audit Results*, and AS 3101, *The Auditor's Report on an Audit of Financial Statements When the Auditor Expresses an Unqualified Opinion*.

[4] *See generally* Section 3 of PCAOB rules, *Auditing and Related Professional Practice Standards*, Part 5, *Ethics and Independence*.

[5] *See* PCAOB, Strategic Plan 2022-2026, at 10, *available at* https://assets.pcaobus.org/pcaob-dev/docs/default-source/about/administration/documents/strategic_plans/strategic-plan-2022-2026.pdf?sfvrsn=b2ec4b6a_4/.

In connection with these initiatives,[6] we analyzed the interim foundational standards that address the general principles and responsibilities of the auditor in conducting an audit. These foundational standards are:

- AS 1001, *Responsibilities and Functions of the Independent Auditor*;
- AS 1005, *Independence*;
- AS 1010, *Training and Proficiency of the Independent Auditor*; and
- AS 1015, *Due Professional Care in the Performance of Work*.[7]

The general principles and responsibilities addressed by the foundational standards include reasonable assurance, due professional care, professional skepticism, independence, competence, and professional judgment. Through this rulemaking, we are reaffirming and modernizing the general principles and responsibilities of the auditor to ensure that the foundation continues to be sound and appropriate for performing high-quality audits.

## A. Rulemaking History

In March 2023, we proposed a new, single standard to replace the foundational standards that address the general principles and responsibilities of the auditor in conducting an audit ("proposed standard").[8] The proposal also included key amendments to other PCAOB standards that address matters that are fundamental to the conduct of an audit. These proposed amendments clarified the engagement partner's responsibility to exercise due professional care related to supervision and review of the audit, accelerated the documentation completion date by reducing the maximum period for the auditor to assemble a complete and final set of audit documentation from 45 days to 14 days, and clarified the auditor's responsibility to evaluate whether the financial statements are "presented fairly."

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[6] *See* PCAOB's interim standards project, *available at* https://pcaobus.org/oversight/standards/standard-setting-research-projects/interim-standards.

[7] When adopted by the Board in 2003, this group of interim standards was designated as AU sec. 110, AU sec. 220, AU sec. 210, and AU sec. 230. In 2015, the PCAOB reorganized its auditing standards using a topical structure and a single, integrated number system, and these interim standards were designated as AS 1001, AS 1005, AS 1010, and AS 1015, respectively. *See Reorganization of PCAOB Auditing Standards and Related Amendments to PCAOB Standards and Rules*, PCAOB Rel. No. 2015-002 (Mar. 31, 2015). The reorganization did not impose additional requirements on auditors or change substantively the requirements of PCAOB standards.

[8] *Proposed Auditing Standard – General Responsibilities of the Auditor in Conducting an Audit and Proposed Amendments to PCAOB Standards*, PCAOB Rel. No. 2023-001 (Mar. 28, 2023) ("proposal" or "proposing release").

We received 28 comment letters on the proposal.[9] Commenters included investor-related groups, firms, firm-related groups, academics, and others. We have considered all comments in developing the final standard and amendments, and specific comments are discussed in the analysis that follows.

## B. Overview of Existing Requirements

This section discusses key provisions of the existing standards.

Key provisions of AS 1001, *Responsibilities and Functions of the Independent Auditor*, include:

- The objective of an audit of financial statements is to express an opinion on the fairness of the financial statements in presenting, in all material respects, the financial position, results of operations, and cash flows in accordance with generally accepted accounting principles ("GAAP"). The auditor also disclaims an opinion if circumstances require. (AS 1001.01)

- The responsibilities of the auditor and management are that (i) the auditor plans and performs the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement, whether caused by error or fraud; and (ii) management is responsible for the financial statements, including adopting accounting policies and establishing and maintaining internal control to initiate, record, process, and report transactions (as well as events and conditions) consistent with management's assertions in the financial statements. (AS 1001.02-.03)

- The auditor is to possess professional qualifications and exercise professional judgment in determining which auditing procedures are necessary in the circumstances to gain a reasonable basis for the opinion. (AS 1001.04-.05)

- The auditor should be aware of and consider auditing interpretations applicable to the audit and, if the guidance in the interpretations is not followed, be prepared to explain how the auditor complied with the provisions of the auditing standard addressed by the guidance. (AS 1001.11)

[9] The comment letters received on the proposal are available in the docket for this rulemaking on the PCAOB's website (https://pcaobus.org/about/rules-rulemaking/rulemaking-dockets/docket-049-responsibilities-auditor-conducting-audit/comment-letters).

Key provisions of AS 1005, *Independence*, require that the auditor:

- Maintain independence in mental attitude and be intellectually honest, impartial, and without bias with respect to the client (i.e., be independent in fact). (AS 1005.01-.03)

- Be free from any obligation to or interest in the client, its management, or its owners, so that the general public maintains confidence in the independence of auditors. (AS 1005.03)

- Not only be independent in fact, but also avoid situations that may lead outsiders to doubt the auditor's independence. (AS 1005.03)

Key provisions of AS 1010, *Training and Proficiency of the Independent Auditor*, require that:

- The audit be performed by persons having adequate technical training, proficiency, and experience as an auditor. (AS 1010.01-.02)

- The training of the auditor be adequate to meet the requirements of the profession, be adequate in technical scope, and include general education. (AS 1010.01-.03)

- New audit professionals obtain professional experience through proper supervision and review of their work by those who are more experienced, with the nature and extent of supervision reflecting variances in practice. (AS 1010.03)

- The engagement partner exercise seasoned judgment in the varying degrees of supervision and review of work performed and judgments exercised by subordinates, and subordinates meet the responsibilities of their work. (AS 1010.03)

- The auditor continue professional training to become aware of developments in business and the profession, and study, understand, and apply new pronouncements on accounting and auditing. (AS 1010.04)

Key provisions of AS 1015, *Due Professional Care in the Performance of Work*, require that:

- The auditor exercise due professional care in the planning and performance of the audit and the preparation of the report, including observance of the auditing standards by professionals within the auditor's organization. (AS 1015.01-.02)

- The auditor possess "the degree of skill commonly possessed" by other auditors and exercise it with "reasonable care and diligence" (i.e., due professional care) in the

planning and performance of the audit and the preparation of the report. (AS 1015.01 and .05)

- The engagement team be assigned to tasks and be supervised commensurate with their level of knowledge, skill, and ability so that they can evaluate the audit evidence they are examining. (AS 1015.06)

- The engagement partner know, at a minimum, the relevant professional accounting and auditing standards, be knowledgeable of the audit client, and be responsible for the assignment of tasks to, and supervision of, the members of the engagement team. (AS 1015.06)

- The auditor exercise professional skepticism throughout the audit, with a questioning mind and a critical assessment of audit evidence, to diligently gather and objectively evaluate audit evidence, and consider the competency and sufficiency of the evidence, and not be satisfied with less than persuasive evidence because of a belief that management is honest. (AS 1015.07-.09)

- The auditor obtain reasonable assurance about whether the financial statements are free of material misstatement, whether caused by error or fraud, or whether any material weaknesses exist as of the date of management's assessment. Reasonable assurance is "a high level of assurance" but is not absolute assurance because of the nature of audit evidence and the characteristics of fraud. (AS 1015.10)

Key provisions of other standards relevant to this rulemaking include:

- AS 1201.04-.05 and AS 2101.03, which describe the engagement partner's responsibilities for supervision and review of audit documentation.

- AS 1215.06, which requires the auditor to document procedures performed, evidence obtained, and conclusions reached with respect to relevant financial statement assertions.

- AS 1215.15, which requires the auditor to complete the necessary auditing procedures and assemble for retention a complete and final set of audit documentation within 45 days after the report release date.

- AS 2810.30, which requires the auditor to evaluate whether the financial statements are presented fairly, in all material respects, in conformity with the applicable financial reporting framework.

- AS 2815, *The Meaning of "Present Fairly in Conformity with Generally Accepted Accounting Principles,"* which explains the meaning of "present fairly" as used in the phrase "present fairly … in conformity with generally accepted accounting

principles," and the basis for the auditor's opinion on whether the financial statements present fairly an entity's financial position, results of operations, and cash flows in conformity with generally accepted accounting principles.

## C. Reasons to Improve Auditing Standards

The new standard and related amendments are intended to modernize, clarify, and streamline the general principles and responsibilities of the auditor described in the foundational standards. We have identified several areas discussed below that we believe will enhance the useability of the requirements by making them easier to read, understand, and apply.

### 1. Alignment with Board-issued Standards and Rules

Since the adoption of the foundational standards, the Board has issued a number of new auditing standards and amendments. Certain of these standards address other principles and responsibilities that are fundamental to the conduct of an audit, including the engagement partner's supervisory and review responsibilities and general requirements for audit documentation. Expressly incorporating these specific principles and responsibilities for conducting an audit in the new standard and related amendments should provide the auditor with more complete direction on matters that are central to the auditor's work.

Certain descriptions of requirements in the foundational standards do not align with the language used in Board-issued standards. For example, some provisions in the foundational standards refer to GAAP;[10] however, in recognition of the SEC's acceptance of filings that include financial statements prepared under accounting frameworks other than U.S. GAAP, such as International Financial Reporting Standards ("IFRS"), Board-issued standards are written as framework neutral and refer instead to the applicable financial reporting framework.[11] As another example, in describing professional skepticism, AS 1015 refers to the competency and sufficiency of the audit evidence rather than using terminology consistent with the Board-issued AS 1105, *Audit Evidence*, which refers to audit evidence as sufficient and appropriate. We believe that aligning the descriptions of the general principles and responsibilities in the new standard with language used in Board-issued standards will minimize potential confusion.

The foundational standards were originally written for audits of financial statements, but certain general principles and responsibilities described in the standards (e.g., reasonable

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[10] *See*, *e.g.*, AS 1001.01 and .03.

[11] *See* paragraph .01, footnote 1 of AS 2410, *Related Parties* ("The auditor should look to the requirements of the U.S. Securities and Exchange Commission for the company under audit with respect to the accounting principles applicable to that company …"); *Auditing Standard No. 18 – Related Parties Amendments to Certain PCAOB Auditing Standards Regarding Significant Unusual Transactions and Other Amendments to PCAOB Auditing Standards*, PCAOB Rel. No. 2014-002 (June 10, 2014), at A4-6 (describing the approach of AS 2410.01, footnote 1 as "framework neutral").

assurance, due professional care, and professional skepticism) apply equally to audits of internal control over financial reporting ("ICFR"). None of the foundational standards mention audits of ICFR or refer to AS 2201, *An Audit of Internal Control Over Financial Reporting That Is Integrated with An Audit of Financial Statements*. While AS 2201 refers to the foundational standards for the requirements related to technical training and proficiency as an auditor, independence, and the exercise of due professional care, including professional skepticism,[12] we believe it is important to clarify in the new standard that the general principles and responsibilities apply to an audit of ICFR as well as an audit of financial statements.

The application of the general principles and responsibilities should be improved by conforming the presentation of the related requirements to the structure used in Board-issued standards. This includes specifying an introduction and objectives to the new standard. In addition, the responsibilities from the foundational standards should be clarified by expressing the related requirements using terms described in PCAOB Rule 3101, *Certain Terms Used in Auditing and Related Professional Practice Standards* (e.g., using "must" and "should" to describe the degree of responsibility that the standards impose on auditors). Much of the explanatory material from the foundational standards that continues to be relevant has been relocated to the discussion in this release, which should facilitate the auditor's navigation of the relevant requirements and align with the approach taken in Board-issued standards.

### 2. New or Revised Independence Requirements Issued by the PCAOB and the SEC

Since the adoption of AS 1005 in 2003, the PCAOB has issued independence rules that have imposed certain incremental independence requirements on firms, relative to the SEC rules[13] (e.g., provisions related to tax services for persons in financial reporting oversight roles at issuer audit clients).[14] These incremental independence requirements are not expressly addressed in AS 1005, but nevertheless the auditor is required to comply with them. Further, while AS 1005 includes a general reference to the SEC's requirements for auditor independence, there is no reference to the specific requirements. We believe it is helpful to refer explicitly in the new standard to the requirements that govern auditor independence, including independence requirements set out by the federal securities laws and related rules, which include an overarching provision for the auditor to maintain independence from its client in fact and in appearance.[15]

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[12] *See* AS 2201.04.

[13] *See generally* PCAOB rules under Section 3. Auditing and Related Professional Practice Standards, Part 5 – Ethics and Independence.

[14] *See* PCAOB Rule 3523, *Tax Services for Persons in Financial Reporting Oversight Roles*.

[15] *See* Section 10A(g) of the Securities Exchange Act of 1934 ("the Exchange Act"), 15 U.S.C. § 78j-1(g); Regulation S-X Rule 2-01, 17 C.F.R. § 210.2-01.

### 3. Advancements in Technology Increasing the Availability of Electronic Audit Tools and Use of Audit Software

Since the foundational standards were adopted by the PCAOB, advancements in technology have increased the availability of electronic audit tools and use of audit software. Auditors have largely moved away from a paper-based approach to audit documentation in favor of using software that houses electronic workpapers and audit programs. Use of electronic workpapers facilitates more efficient performance and review of audit procedures and enables auditors to assemble a complete and final set of audit documentation in less time than in a paper-based environment.

Auditors are also expanding their use of and reliance on electronic audit tools. For example, some firms have made significant investments in internally developed tools for use in the audit. In addition, some "off-the-shelf" applications such as data analysis software have become available to auditors. These advancements have changed the way that many auditors perform and document their audit procedures and retain related audit documentation. Accordingly, the new standard and amendments reflect an accelerated documentation completion date and related documentation requirements.

### 4. Outdated and Inconsistent Language

The foundational standards include outdated and inconsistent language that is not relevant to audits conducted under the standards of the PCAOB. For example, paragraph .03 of AS 1001 provides that the auditor may draft the financial statements in whole or in part based on information from management during performance of the audit. This provision is outdated and should not be included in PCAOB auditing standards because an auditor drafting the financial statements would violate the applicable independence rules.[16] Eliminating outdated language used in the foundational standards should remove inconsistencies between PCAOB auditing standards and the relevant rules of the PCAOB and the SEC. Similarly, in describing the objective of the audit, paragraph .01 of AS 1001 refers to financial position, results of operations, and cash flows. This language could be unnecessarily limiting because the objective of the audit does not change based on the subject matter of the audit (e.g., whether it is an audit of ICFR or the financial statements). The new standard excludes references that are outdated or inconsistent, which we believe improves the application of the requirements and provides clearer direction to auditors in executing their responsibilities.

### 5. Activities of Other Standard Setters

Since the Board's adoption of the foundational standards, both the International Auditing and Assurance Standards Board ("IAASB") and the Auditing Standards Board ("ASB") of the AICPA have updated their analogous standards:

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[16] *See* Regulation S-X Rule 2-01(c)(4)(i), 17 C.F.R. § 210.2-01(c)(4)(i).

- IAASB Standard – International Standard on Auditing 200, *Overall Objectives of the Independent Auditor and the Conduct of an Audit in Accordance with International Standards on Auditing* ("ISA 200") (effective 2009); and

- ASB Standard – AU-C Section 200, *Overall Objectives of the Independent Auditor and the Conduct of an Audit in Accordance With Generally Accepted Auditing Standards* ("AU-C 200") (effective 2012).

These revisions were part of clarity projects that were designed to make the standards easier to read, understand, and apply.[17] These standards were updated to align the terminology used throughout the standards for consistency and to enhance and update explanatory materials.

### 6. Comments on Reasons for Standard Setting and Proposed Approach

The proposal sought comment on the appropriateness of the general principles and responsibilities of the auditor and the approach to reorganize and consolidate those responsibilities. Commenters who responded generally agreed that the general principles and responsibilities (i.e., reasonable assurance, due professional care, professional skepticism, independence, competence, and professional judgment) described in the proposal are appropriate. One commenter suggested that we address the relevance and reliability of audit evidence and information in conjunction with the requirements in AS 1105, as part of the general principles and responsibilities. Some commenters addressed the reorganization and consolidation of the four existing foundational standards into one new standard and generally supported the proposed approach.

Commenters were generally supportive of the Board's efforts to modernize and streamline the general principles and responsibilities of the auditor. Several commenters, for example, agreed that the proposed standard would provide a more logical presentation, which would enhance the useability of the standards by making them easier to read, understand, and apply. Some commenters, including investor-related groups, also expressed support for the proposal's focus on investor protection.

Two commenters suggested consideration of analogous standards of the IAASB and the ASB. One commenter stated that PCAOB auditing standards should not diverge from AICPA auditing standards, to the extent appropriate. Another commenter recommended that we consider similar standards of the IAASB and the ASB and assess whether their approach could result in higher quality audits.

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[17] Descriptions of the clarity projects of the IAASB and ASB are available, respectively, at https://www.iaasb.org/projects/clarity-iaasb-standards and https://us.aicpa.org/interestareas/frc/auditattest/improvingclarityasbstandards.

The proposal also sought comment on the appropriateness of the general principles and responsibilities of the auditor in light of the availability of electronic audit tools and the use of audit software by both larger and smaller firms. Most commenters did not address this question. One commenter agreed that the proposed general principles and responsibilities of the auditor are appropriate and clear because they are necessary to the audit regardless of electronic tools and audit software. Another commenter recommended considering future possibilities and uses of machine learning and artificial intelligence ("AI") technologies, which in the views of the commenter "are progressing rapidly."

The final standard retains the general principles and responsibilities of the auditor described in the proposal, subject to revisions described below. The final standard also retains the overall approach of consolidating the foundational standards and the general principles and responsibilities of the auditor under one standard. We did not add specific requirements for evaluating the relevance and reliability of audit evidence, as suggested by one commenter, because AS 1105 provides the necessary framework for this evaluation. The final standard includes general requirements for conducting an audit, and obtaining sufficient appropriate audit evidence is part of those general requirements.

In addition, in the final standard we did not add provisions specific to the current and future use of emerging technologies. Due to the ever-evolving nature of technology, specifying requirements for certain types of technology based on how those tools are used today could quickly make the standard become outdated. Further, the general principles and responsibilities addressed in the standard apply to all audits, irrespective of the technology that may be used in performing audit procedures. We continue to address emerging technologies (e.g., machine learning and AI) as part of the staff's ongoing Data and Technology research project.[18] Research from this project may give rise to individual standard-setting projects and may also inform the scope or nature of other projects that are included on our standard-setting agenda.

With respect to comments on analogous standards issued by other standard setters, we believe that AS 1000 is based on general principles and responsibilities of the auditor, similar to the bases of analogous IAASB and AICPA standards. We carefully considered the approaches of other standard setters when developing the proposal, and the new standard and amendments being adopted reflect the approach that we believe best protects investors and furthers the public interest. As a result, certain differences exist between our new standard and those of other standard setters, including a number of provisions that we believe are appropriate and consistent with our statutory mandate to protect the interests of investors and further the public interest.

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[18] *See* the PCAOB's agenda related to standard setting, research, and rulemaking projects, *available at* https://pcaobus.org/oversight/standards/standard-setting-research-projects.

# III. DISCUSSION OF FINAL RULES

## A. Overview of Final Rules

We are replacing AS 1001, AS 1005, AS 1010, and AS 1015 with one standard, AS 1000, that describes the general principles and responsibilities of an auditor[19] in conducting an audit in accordance with the standards of the PCAOB. Briefly, the new standard:

- Includes introductory language that reaffirms the auditor's fundamental obligation to protect investors through the preparation and issuance of informative, accurate, and independent auditor's reports;

- Includes objectives for the auditor to conduct and communicate the results of both an audit of a company's financial statements and an audit of a company's ICFR and satisfy and fulfill other general principles and responsibilities described in this standard;

- Retains and clarifies the general principles and responsibilities that are important for an audit, including reasonable assurance, due professional care, professional skepticism, and professional judgment;

- Aligns the engagement partner's supervisory responsibilities under AS 1201 with due professional care;

- Retains the requirement for the auditor to be independent but expresses the obligation more directly by referring to the PCAOB's independence criteria in its rules and standards, and the independence criteria set out in the rules and regulations of the SEC;

- Describes the auditor's obligations to (i) comply with ethics requirements, (ii) obtain and maintain competence, and (iii) prepare audit documentation;

- Expresses the auditor's responsibilities by using the terms set forth in PCAOB Rule 3101 (e.g., must and should) that describe the degree of responsibility that PCAOB standards impose on auditors; and

- Removes language that is outdated, inconsistent, and not relevant to audits conducted under the standards of the PCAOB.

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[19] The term "auditor" includes both a public accounting firm registered with the PCAOB and associated persons thereof, as defined in PCAOB Rule 1001, *Definitions of Terms Employed in Rules*. For example, engagement quality reviewers ("EQRs"), by virtue of their status as associated persons, are within the term "auditor" in AS 1000. *See also* paragraph .03 of AS 1220, *Engagement Quality Review*.

As previously noted, we are amending other PCAOB auditing standards that address responsibilities fundamental to the conduct of an audit to:

- Clarify the engagement partner's existing responsibilities for supervision and review in AS 1201, AS 1215, and AS 2101 to provide more specificity about the engagement partner's responsibility to exercise due professional care related to supervisory and review activities required to be performed under existing auditor requirements;

- Clarify the requirements for audit documentation in AS 1215 to identify who performed the work, who reviewed the work, and the date of such review;

- Accelerate the period in AS 1215 to assemble a complete and final set of audit documentation for retention from 45 days to 14 days; and

- Update and incorporate the underlying requirements of AS 2815 into AS 2810, and rescind AS 2815, while preserving the meaning of "present fairly" and streamlining the requirements to provide a more logical presentation.

In a separate release, the Board is also adopting a new quality control standard, QC 1000, *A Firm's System of Quality Control*, and a new ethics standard, EI 1000, *Integrity and Objectivity*, together with other amendments to PCAOB standards, rules, and forms.[20] This release includes references to QC 1000 and EI 1000, where appropriate.

## B. AS 1000

### 1. Introduction

*See paragraphs .01 through .02 of the new standard in Appendix 1.*

The first paragraph of the proposed standard, under the heading "Introduction," described the fundamental obligation of auditors to protect investors through the preparation and issuance of informative, accurate, and independent auditor's reports. It noted that an audit primarily benefits investors who rely on the audit to provide objective and independent opinions on whether the company's financial statements are presented fairly and, if applicable, on the effectiveness of the company's ICFR. The proposed paragraph further provided that a properly conducted audit and related auditor's report enhance the confidence of investors and other market participants in the company's financial statements and, if applicable, ICFR. The existing foundational standards do not include an introduction and do not describe the auditor's fundamental responsibility to protect investors.

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[20] *See A Firm's System of Quality Control and Other Amendments to PCAOB Standard, Rules, and Forms*, PCAOB Rel. No. 2024-005 (May 13, 2024).

Investor-related groups strongly supported the proposed standard's emphasis on the auditor's obligation to protect investors. These commenters suggested some clarification in the language describing the auditor's obligation for, and role in, protecting investors, as described in the Supreme Court opinion in *United States v. Arthur Young & Co*.[21] Some pointed to, for example, language stating that the auditor "assumes a *public* responsibility transcending any employment relationship with the client" and that the auditor "owes ultimate allegiance to the corporation's creditors and stockholders, as well as the investing public."[22] One of these commenters stated that without additional clarification, the phrase "fundamental obligation" is a vague concept and open to interpretation. Two commenters recommended including in AS 1000 a footnote from the proposal that cites the *Arthur Young* opinion.

Two commenters, including an investor-related group, recommended that the standard's reference to investors be broadened to include shareholders, debtholders, and other financial statement users who rely on a company's financial statements, consistent with the usage by Financial Accounting Standards Board ("FASB") and the Supreme Court in the *Arthur Young* opinion. One of these commenters recommended including a definition of "financial statement users" in the final standard. Another recommended adding a footnote to the first sentence of paragraph .01 defining and describing the meaning of "investors."

A number of other commenters, primarily firms, expressed concerns that the introduction language describing the auditor's role was unclear and could be misleading. For example, several commenters noted that the description of the auditor's role in protecting investors could be viewed as creating a new legal obligation owed to investors. In the view of one commenter, the proposed language implied that investor protection is the sole responsibility of the auditor and could give investors false confidence that they can solely rely on an auditor's report as investment advice, when in fact there are many other factors investors should consider. Another commenter asserted that the proposed language could create a misimpression that auditors are permitted and expected to deviate from auditing standards when they believe such a departure would be warranted to further investors' interests. These commenters suggested that the Board clarify the introduction language in the final standard. Some commenters provided alternative language for the Board's consideration. For example, two commenters suggested replacing the phrase "properly conducted" in the last sentence of paragraph .01 with "conducted in accordance with the standards of the PCAOB" to align with language used in the auditor's report. One commenter suggested deleting paragraph .01 entirely.

After considering the comments received, we are retaining the proposed approach to the introduction section, while making certain revisions in light of the comments received.

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[21] *United States v. Arthur Young & Co.*, 465 U.S. 805, 817-18 (1984).

[22] *Id.* at 817 (emphasis in original).

We have revised the first sentence of the introduction to state that the auditor has a fundamental obligation to protect investors through the preparation and issuance of informative, accurate, and independent auditor's reports. We also removed a redundant statement from proposed paragraph .01 ("and that obligation governs the auditor's work under the standards of the PCAOB"). This statement is unnecessary because paragraph .02 already clarifies that AS 1000 describes the general principles and responsibilities of the auditor in properly conducting an audit in accordance with the standards of the PCAOB. This includes the fundamental obligation to protect investors as described in paragraph .01.

The fundamental obligation to protect investors is interwoven in the general principles and responsibilities that guide auditors throughout their work. Under current law, the auditor plays a critical role in the financial reporting process. By issuing opinions concerning whether financial statements are presented fairly, in all material respects, in conformity with the applicable financial reporting framework, auditors serve a special "public watchdog" function under the existing federal securities laws, requiring "complete fidelity to the public trust."[23] As "gatekeepers," auditors have a public responsibility to serve the public interest.[24] Investors rely on auditors to promote companies' adherence to federal securities law mandates and companies' disclosure of accurate and reliable financial information.[25] "Investor confidence is bolstered by the knowledge that public financial statements have been subjected to the rigors of independent and objective investigation and analysis" by an auditor.[26] This enhanced confidence of investors and other financial statement users in the company's financial statements and ICFR also plays an integral role in maintaining the public trust in the capital markets. The introduction in the final standard underscores the auditor's obligation under our auditing standards and other applicable laws and regulations.

We emphasize – in response to commenters who expressed concern that the introductory language, and specifically its use of the term "obligation," could be interpreted to establish a new legal duty – that the introductory language does not alter any existing regulatory or legal requirements or obligations between auditors and investors. It does not establish a novel duty or new form of legal obligation. Rather, it reaffirms the auditor's

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[23] *Arthur Young*, 465 U.S. at 817-18.

[24] *In the Matter of KPMG Peat Marwick LLP*, SEC Rel. No. 34-43862, at 14 & n.54 (Jan. 19, 2001); *see* John C. Coffee Jr., *Gatekeepers: The Professions and Corporate Governance* 2-3 (2006) (describing "gatekeepers" as "repeat players who provide certification or verification services to investors, vouching for someone else who has a greater incentive than they to deceive").

[25] *In the Matter of the Application of S.W. Hatfield, C.P.A.*, SEC Rel. No. 34-69930, at 33 (July 3, 2013) (reviewing PCAOB disciplinary action).

[26] *McCurdy v. SEC*, 396 F.3d 1258, 1261 (D.C. Cir. 2005); *see Arthur Young*, 465 U.S. at 819 n.15.

obligation under the existing legal framework and the important role of the auditing profession in our capital markets.[27]

Paragraph .01 of the final standard has also been revised, as suggested by some commenters, to state that the auditor's responsibility[28] transcends the auditor's relationship with management and the audit committee of the company under audit, providing the foundation for an objective and independent audit. This statement expresses a longstanding principle of public accounting.[29] Paragraph .01 also states that a properly conducted audit and the related auditor's report enhance the confidence of investors and other financial statement users in the company's financial statements and, if applicable, ICFR. We have retained the phrase "properly conducted audit" to align with the description in paragraph .02. We removed the sentence that states that "An audit primarily benefits investors, who rely on the audit to provide an objective and independent opinion on whether the company's financial statements are presented fairly and, if applicable, on the effectiveness of the company's internal control over financial reporting" because it is redundant and unnecessary in the context of the surrounding statements. We do not believe that the language in paragraph .01 suggests that auditors may deviate from PCAOB auditing standards to protect investors. In fact, the language clearly establishes the fundamental duty of auditors to prepare and issue their reports in accordance with PCAOB standards. Similarly, we do not interpret the language of paragraph .01 as suggesting that investors should view auditor's reports as the sole source of investment advice. Collectively, these provisions emphasize that auditors play a critical role in ensuring the accuracy and transparency of a company's financial information, and that this role helps investors make well-informed decisions and supports trust in a company's financial statements.

Finally, a new footnote to paragraph .01 clarifies that references to "investors and other financial statement users" in AS 1000 encompass a broad spectrum of stakeholders. This group

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[27] *See* Section 101(c)(6) of the Sarbanes-Oxley Act of 2002 (authorizing PCAOB to enforce compliance with the "Act, the rules of the Board, professional standards, and the securities laws relating to the preparation and issuance of audit reports and the *obligations* and liabilities of accountants with respect thereto, by registered public accounting firms and associated persons thereof ….") (emphasis added).

[28] The terms "obligation" and "responsibility" are used synonymously in this standard.

[29] *See Arthur Young*, 465 U.S. at 817-818 ("By certifying the public reports that collectively depict a corporation's financial status, the independent auditor assumes a *public* responsibility transcending any employment relationship with the client. The independent public accountant performing this special function owes ultimate allegiance to the corporation's creditors and stockholders, as well as to the investing public.") (emphasis in original); AICPA Professional Standards, Vol. 2, Code of Professional Conduct, ET Section 53, Article II – The Public Interest (2002) (".01 A distinguishing mark of a profession is acceptance of its responsibility to the public. The accounting profession's public consists of clients, credit grantors, governments, employers, investors, the business and financial community, and others who rely on the objectivity and integrity of certified public accountants to maintain the orderly functioning of commerce.").

includes not only a company's existing and potential shareholders, but also bondholders, lenders, other creditors, and others who use the company's financial statements.[30]

In addition to the revisions to paragraph .01, we relocated certain content, discussed in more detail below, from proposed paragraph .15 into a new note to paragraph .01. The note reminds auditors that their obligation to protect investors provides important context to the auditor's work when applying the requirements of AS 1000 and other PCAOB standards and rules (e.g., when conducting interim reviews in accordance with AS 4105, *Reviews of Interim Financial Information*, or when conducting audits of ICFR in accordance with AS 2201).

Paragraph .02 summarizes the scope and content of AS 1000. We did not receive comment on this paragraph and are adopting it as proposed.

### 2. Objectives of the Auditor

*See paragraph .03 of the new standard in Appendix 1.*

The proposed standard set forth three objectives of the auditor (a) in an audit of financial statements, to obtain reasonable assurance about whether the financial statements are free of material misstatement, whether due to error or fraud, and to issue an auditor's report that expresses an opinion about whether the financial statements, taken as a whole, are presented fairly, in all material respects, in conformity with the applicable financial reporting framework; (b) in an audit of internal control over financial reporting, to obtain reasonable assurance about whether material weaknesses exist as of the date specified in management's assessment, and to issue an auditor's report that expresses an opinion on the effectiveness of the company's internal control over financial reporting; and (c) to communicate externally, as required by applicable professional and legal requirements. Other than AS 1001,[31] the existing foundational standards do not include an objective.

The proposal defined the term "applicable professional and legal requirements" by referring to the term's definition in proposed QC 1000.[32] That proposed definition included (i) professional standards, as defined in PCAOB Rule 1001(p)(vi); (ii) rules of the PCAOB that are not professional standards; and (iii) to the extent related to the obligations and responsibilities of accountants or auditors or to the conduct of engagements, rules of the SEC, other provisions

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[30] *See* FASB, Statement of Financial Accounting Concepts No. 8, *Conceptual Framework for Financial Reporting*, Chapter 1, *The Objective of General Purpose Financial Reporting* (Dec. 2021) ("The objective of general purpose financial reporting is to provide financial information about the reporting entity that is useful to existing and potential investors, lenders, and other creditors in making decisions about providing resources to the entity").

[31] *See* AS 1001.01.

[32] *See A Firm's System of Quality Control and Other Proposed Amendments to PCAOB Standards, Rules, and Forms*, PCAOB Rel. No. 2022-006 (Nov. 18, 2022).

of U.S. federal securities law, and other applicable statutory, regulatory, and other legal requirements.

Several commenters expressly supported the proposed objectives of the auditor. Some commenters suggested ways to further clarify these objectives. For example, one commenter suggested that the objectives be reframed as objectives of the "audit" rather than of the "auditor." Another commenter suggested moving the requirements on the determination of critical audit matters ("CAMs") from AS 3101.11, to the objectives of the auditor in AS 1000 in order to highlight the importance of CAMs. One commenter recommended that the objective related to the audit of ICFR refer to the relevant criteria used (e.g., criteria issued by the Committee of Sponsoring Organizations of the Treadway Commission) and clarify that it is integrated with the audit of financial statements.

With respect to the communication objective, one commenter stated that the proposed objective should also refer to communications with the company. Another commenter stated that the term "applicable legal and professional requirements" is overly broad and may inadvertently scope in legal requirements outside of public accountancy laws. An additional commenter suggested that AS 1000 refer instead to "PCAOB rules and standards."

We are adopting the objectives in the final standard substantially as proposed, with the modifications discussed below.

The purpose of the objectives is to provide additional context for understanding the requirements in the standard. Therefore, we added the objective to "satisfy and fulfill the other general principles and responsibilities described in this standard." This provides more explicit linkage to the general principles and responsibilities set forth in the final standard.

The objectives refer, as proposed, to the "objectives of the auditor." Because the standard addresses the general principles and responsibilities of the auditor in conducting an audit, we believe that the objectives should be directed at the "auditor" rather than the audit as a whole.

The determination of CAMs is an important part of the auditor's reporting responsibilities and is encompassed under the applicable professional and legal requirements. The auditor's responsibilities for determining and communicating CAMs are described in AS 3101 and align with the stated objectives of that standard.[33] Rather than repeating these requirements, we have instead added a note to paragraph .17 of the final standard that refers to the potential inclusion of CAMs in the auditor's report (see Section III.B.6).

The suggested references to the relevant criteria used in the audit of ICFR are not suitable for the objective section of AS 1000 and are already covered in other PCAOB standards. The specific requirements relevant to performing an audit of ICFR are addressed in AS 2201,

[33] *See* AS 3101.04 and .11-.17.

which provides the appropriate context for the framework to be used by the auditor when conducting an ICFR audit and integrating the audit of ICFR with an audit of financial statements.

As was proposed, the final standard includes an objective to communicate externally in accordance with applicable legal and professional requirements. The auditor has a responsibility to make certain communications (e.g., communications about audit results to the audit committee under AS 1301, *Communications with Audit Committees*), in addition to reporting externally on the results of the audit. The reference to these requirements in the objective is not intended to limit or preclude appropriate communications with company personnel. For example, PCAOB auditing standards require the auditor to conduct various inquiries of management and other company personnel (e.g., AS 2110, *Identifying and Assessing Risks of Material Misstatement*, and AS 2201), which is part of complying with applicable professional and legal requirements.

For ease of reference, the final standard includes the definition of the term "applicable professional and legal requirements," in Appendix A as:

- Professional standards, as defined in PCAOB Rule 1001(p)(vi);
- Rules of the PCAOB that are not professional standards; and
- To the extent related to the obligations and responsibilities of accountants or auditors in the conduct of engagements or in relation to the quality control system, rules of the SEC, other provisions of U.S. federal securities law, ethics laws and regulations, and other applicable statutory, regulatory, and other legal requirements.

This definition is intended to capture all professional and legal requirements specifically related to engagements under PCAOB standards of issuers and SEC-registered broker-dealers, including relevant accounting, auditing, and attestation standards, PCAOB rules, SEC rules and regulations, other provisions of federal securities law, other relevant laws and regulations (e.g., state law and rules governing accountants), applicable ethics law and rules, and other legal requirements related to the obligations and responsibilities of accountants or auditors in the conduct of the firm's engagements or in relation to the quality control system.[34] It does not

[34] The requirements related to compliance with applicable professional and legal requirements are meant to make clear that, in engagements subject to PCAOB auditing standards, all applicable professional and legal requirements must be followed. The requirement does not suggest that application of "other applicable statutory, regulatory, and other legal requirements" could supersede rules of the SEC, other provisions of U.S. federal securities law, rules of the PCAOB that are not professional standards, or PCAOB professional standards. On the contrary, requirements relating to "applicable professional and legal requirements" are meant to highlight the importance of adhering to other requirements when those requirements do not conflict with or abridge requirements of federal securities laws, PCAOB rules, or PCAOB standards.

encompass requirements that apply to businesses generally, such as tax laws, safety regulations, and employment law.

This definition reflects revisions made in response to comments received on proposed QC 1000.[35] The definition was expanded to explicitly mention ethics laws and regulations.[36] It was also refined to make clear that it encompasses statutory, regulatory, and other legal requirements beyond professional standards and other PCAOB rules "[t]o the extent related to the obligations and responsibilities of accountants or auditors in the conduct of engagements or in relation to the quality control system." This change is designed to limit the breadth of the definition to the relevant circumstances. The phrase "quality control policies and procedures," used in PCAOB Rule 1001(p)(vi), is drawn from Section 110(5) of Sarbanes-Oxley Act of 2002 ("Sarbanes-Oxley"), and therefore no amendment to the PCAOB rule was necessary.

### 3. Professional Qualifications of the Auditor

#### i. Independence

*See paragraphs .04 through .05 of the new standard in Appendix 1.*

We proposed to carry forward the existing requirement in AS 1005 for the auditor to be independent, and to align the language that describes auditor independence obligations with language used in PCAOB Rule 3520, *Auditor Independence*, and SEC Rule 2-01.[37] Specifically, we proposed to require the auditor to be independent of its audit client both in fact and in appearance throughout the audit and professional engagement period.[38] The proposed standard also clarified that the auditor is not independent with respect to an audit client if the auditor is not, or a reasonable investor with knowledge of all relevant facts and circumstances would conclude that the auditor is not, capable of exercising objective and impartial judgment on all matters encompassed within the engagement. This clarification aligned the standard with

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[35] Two commenters supported the definition as proposed. One commenter recommended including the profession's ethical standards explicitly. Two commenters stated the phrase "other applicable statutory, regulatory, and other legal requirements" could be read broadly and extend beyond regulations that directly bear on the conduct of audit engagements. Another commenter suggested amending the definition of "professional standards" in PCAOB Rule 1001(p)(vi) to refer to "quality control standards" rather than "quality control policy and procedures."

[36] These include those arising under state law or the law of other jurisdictions (e.g., obligations regarding client confidentiality).

[37] Regulation S-X Rule 2-01, 17 C.F.R. § 210.2-01.

[38] *See* PCAOB Rule 3501, *Definitions of Terms Employed in Section 3, Part 5 of the Rules*, for the definition of the term "audit and professional engagement period."

language used in SEC Rule 2-01(b)[39] to explain further the meaning of being independent both in fact and in appearance. In addition, we proposed to require the auditor to satisfy the independence criteria set out in the rules and standards of the PCAOB, and satisfy all other independence criteria applicable to the engagement, including the independence criteria set out in the rules and regulations of the SEC under the federal securities laws.

Several commenters expressed support for including in AS 1000 the existing requirements from AS 1005 and stating more directly the auditor's obligation to comply with the independence requirements of the PCAOB and SEC. Two commenters, including an investor-related group, suggested that we replace references to "audit client" with "company under audit." One commenter asserted that using "client" does not recognize that the auditor's public responsibility transcends the employment relationship with the client. Another commenter asserted that the use of "client" mischaracterizes the relationship between auditor and the company or its management, and places the auditor in a "subservient" position. In addition, one commenter suggested adding to the final standard additional language from SEC Rule 2-01(b) to indicate that the PCAOB and SEC will consider "all relevant facts and circumstances" in determining independence. That commenter also suggested limiting the use of the term "independent" in the title of the auditor's report to only those auditors that have complied with the SEC and PCAOB rules.

After considering the comments received, we are adopting the requirements related to independence substantially as proposed with some modifications. We agree with the commenters' observation that language used in our standards can help emphasize that audits are performed primarily for the benefit of investors, not management of the company. Accordingly, we have replaced references to "audit client" with "company under audit" and added a footnote to clarify that the phrase "company under audit" has the same meaning as "audit client" as defined by PCAOB Rule 3501(a)(iv).

We did not add to the final standard additional language from SEC Rule 2-01(b) stating that the PCAOB and SEC will consider "all relevant facts and circumstances" in determining independence. Our standards do not address the SEC's processes, and we need not repeat in this standard that relevant matters are considered in PCAOB independence determinations.[40]

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[39] Under the general standard in SEC Rule 2-01(b), the SEC "will not recognize an accountant as independent, with respect to an audit client, if the accountant is not, or a reasonable investor with knowledge of all relevant facts and circumstances would conclude that the accountant is not, capable of exercising objective and impartial judgment on all issues encompassed within the accountant's engagement."

[40] *See* Note to paragraph (b) of PCAOB Rule 3525, *Audit Committee Pre-approval of Non-audit Services Related to Internal Control Over Financial Reporting* ("Independence requirements provide that an auditor is not independent of his or her audit client if the auditor is not, or a reasonable investor with *knowledge of all relevant facts and circumstances* would conclude that the auditor is not, capable of

We also did not add limitations on the use of the term "independent" in the title of the auditor's report. AS 3101 contains requirements regarding the content of the auditor's report, including the title "Report of Independent Registered Public Accounting Firm." AS 3101 also requires that the auditor's report include a statement that the auditor is required to be independent with respect to the company in accordance with U.S. federal securities laws and the applicable rules and regulations of the SEC and PCAOB. Imposing any limitations on the use of the term "independent" in the title, as suggested by a commenter, is outside of the scope of this standard.

### ii. Ethics

*See paragraph .06 of the new standard in Appendix 1.*

We proposed to require the auditor to comply with applicable ethics requirements, including the rules and standards of the PCAOB. Under the proposed standard, ethics requirements included the rules in Section 3, Part 5 of PCAOB rules and proposed EI 1000, *Integrity and Objectivity,* of the QC proposal. The existing foundational standards do not reference the auditor's responsibility to comply with ethics requirements.

A few commenters suggested revisions to the proposed requirement. Two commenters, including an investor-related group, stated that the proposed requirement is weak because it focused on merely complying with rules and standards of the Board. The investor-related group also suggested adding language that discusses subordination of judgment to others, specifically those outside the audit firm (e.g., external specialists). The other commenter recommended requiring that firms create and maintain codes of ethics embracing the principles of proposed EI 1000 and upholding the integrity of capital markets and auditors' fundamental obligations to investors. An additional commenter suggested addressing in the standard broader ethical principles, such as integrity and objectivity, in addition to compliance with rules and standards.

After considering the comments received, we are retaining the requirement to comply with ethics requirements substantially as proposed, with the modifications discussed below. We have added the word "ethics" before "rules and standards of the PCAOB" to provide a clearer indication of the rules and standards we are referencing. Under the final standard, applicable ethics requirements are not limited to the ethics rules and standards of the PCAOB but also include state law and the laws of other jurisdictions that may establish additional ethics provisions with which the auditor is required to comply (e.g., obligations regarding conflicts of interest).

We agree with the underlying point of the comment that auditors should not subordinate their judgment to individuals outside the audit firm (e.g., external specialists) and believe that the new standard will achieve the desired objective of the comment. A

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exercising objective and impartial judgment on all issues encompassed within the accountant's engagement.") (emphasis added).

subordination or relinquishment of professional judgment would be inconsistent with the requirements of AS 1000.09-.10 related to due professional care, which are discussed in Section III.B.4 below. In addition, EI 1000 addresses the broader ethical principles of integrity and objectivity. Specifically, the overarching requirements in EI 1000 include (i) maintaining integrity, which includes being honest and candid, not knowingly or recklessly misrepresenting facts, and not subordinating judgment; and (ii) maintaining objectivity, which includes being impartial, intellectually honest, and free of conflicts of interest. The intent of the requirement to comply with ethics in AS 1000 is to remind auditors of their responsibilities described in EI 1000 and Section 3, Part 5 of PCAOB rules. Therefore, additional discussion of broader ethical principles and responsibilities is appropriately addressed in EI 1000 and need not be duplicated in AS 1000. We have expanded the reference to EI 1000 in footnote 6 of paragraph .06 of AS 1000 to clarify that EI 1000 specifically requires auditors to maintain integrity and objectivity. Further clarification on matters related to subordination of professional judgment is unnecessary in this release. Lastly, we considered comments related to firms' adoption of an ethics code as part of the adoption of EI 1000.

#### iii. Competence

*See paragraphs .07 and .08 of the new standard in Appendix 1.*

##### a. Description of competence

We proposed to require that the audit be performed by an auditor who has competence to conduct an audit in accordance with applicable professional and legal requirements. Competence, as described in the proposed standard, consists of having the knowledge, skill, and ability that enable an auditor to perform the assigned activities in accordance with applicable professional and legal requirements and the firm's policies and procedures. In the proposing release, we explained that the auditor's knowledge and skill relate to adequate technical training and proficiency as an auditor, and the auditor's ability relates to the capabilities to perform, and in the case of supervisory staff, to review assigned tasks. The proposed standard also provided that, in determining the appropriate level of competence, the measure is qualitative rather than quantitative because quantitative measurement may not accurately reflect the experience gained over time. A note to the proposed requirement stated that competence includes knowledge and expertise in accounting and auditing standards and in SEC rules and regulations relevant to the company being audited and to the related industry or industries in which it operates. The proposed requirement was consistent with the auditor's existing responsibilities under AS 1010 for maintaining "adequate technical training and proficiency" but used updated terminology.

Several commenters sought greater clarity in the proposed requirement, stating that it did not account for the collective competence of the engagement team or that it might imply that all individual members of an engagement team are expected to have the same level of competence. These commenters generally suggested (i) revising the requirement to apply to, for example, "the engagement team, including specialists" or "auditors, collectively" instead of

"an auditor" and (ii) clarifying that necessary competence is commensurate with the assigned tasks of the individual auditor. One commenter suggested (i) defining the individuals intended to be covered by the requirement, including subject matter experts and EQRs; (ii) explaining that the competence of individuals varies based on a variety of factors; and (iii) including quantitative factors in the measure of competence. Another commenter noted that the proposed requirement could be interpreted to limit the ability to assign challenging work to junior staff because they may lack significant experience.

Some commenters, mostly firms and professional organizations, also expressed concern with the description of competence in the note to the proposed requirement – which referred to having "expertise" in SEC rules and regulations and the relevant industry of the company being audited – and asked for additional clarification. These commenters asserted that the term "expertise" may impose a higher standard of competence than intended and could imply that the expected level of knowledge is that of a person qualified to engage in the practice of another profession or occupation (e.g., the legal profession). One of these commenters also expressed concern with the implication that a partner without relevant expertise in the industry in which the issuer operates may not be competent to perform an audit of the issuer, even with the assistance of other firm or engagement team members with relevant industry expertise. Several commenters recommended deleting the reference to "expertise" or using alternative language such as "proficiency" or "sufficient knowledge."

After considering the comments received, we are adopting the requirement related to competence substantially as proposed, with the modifications discussed below.

First, consistent with our description in the proposal, we continue to believe the level of competence needed to conduct the audit is driven by the activities assigned to the individual auditors performing those activities. As the assigned activities in an audit vary from individual to individual, so does the required level of competence to complete those activities in accordance with applicable professional and legal requirements and the firm's policies and procedures. For example, a first-year auditor is not expected to have the same level of competence as a more experienced auditor because the tasks assigned to the seasoned auditor generally require experience gained over time. Further, PCAOB standards and rules use the term "auditor" to mean both a firm registered with the PCAOB and its associated persons.[41] Therefore, we believe that defining the individuals covered by the requirement or revising terminology to "auditors" or "engagement team," as suggested by some commenters, is not necessary. The requirements regarding the appropriate assignment of responsibilities to engagement team members and proper supervision are addressed in other PCAOB standards.[42]

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[41] *See* PCAOB Rule 1001(a)(xii).

[42] *See, e.g.*, paragraph .05 of AS 2301, *The Auditor's Responses to the Risks of Material Misstatement*, and AS 1201.05.

Second, we agree that quantitative measures are not wholly irrelevant when measuring competence. Quantitative measures alone may not accurately reflect the nature of experience gained over time and therefore competence should not be measured exclusively on a quantitative basis.[43] In consideration of comments, the final requirement clarifies that competence is measured both qualitatively and quantitatively.

Third, the intent of the proposed requirement's note (providing that competence "includes knowledge and expertise" in certain areas) was to provide additional direction to auditors on the meaning of competence in the context of the company being audited. We did not intend to impose a higher standard of competence beyond having the knowledge, skill, and ability to enable the auditor to perform the assigned activities in accordance with applicable professional and legal requirements. We have therefore changed "expertise" to "proficiency" in the final requirement in response to comments. Nevertheless, we continue to believe that understanding the company's business and being proficient in the rules and regulations relevant to the company under audit and its related industry is an important part of competence. For example, an engagement partner with significant experience mostly in auditing manufacturing companies may not necessarily have the appropriate level of competence to oversee, and have primary responsibility for, an audit of a financial institution.

### b. Developing and maintaining competence

We also proposed to require that the auditor develop and maintain competence through an appropriate combination of academic education; professional experience in accounting and auditing with proper supervision; and training, including accounting, auditing, independence, ethics, and other relevant continuing professional education. Existing AS 1010 includes a similar requirement.

Investor-related groups advocated for the inclusion of investor-related training that focuses on investors as the primary beneficiaries of the audit and being responsive to investors' needs. These commenters also emphasized the importance of including the auditor's understanding of the business and industry related to the company under audit as part of developing competence. One investor-related group suggested specific training on materiality.

We are retaining the requirement to develop and maintain competence as proposed. We agree with investor-related groups' views on the importance of protecting investors when conducting an audit. In that regard, paragraph .01 of the final standard and the related discussion in Section III.B.1 of this release provide the context of investor protection that is relevant to the auditor's compliance with the requirements for developing and maintaining competence. Further, in considering commenters' suggestion about investor-focused training, we believe that the implementation of the final standard will necessarily involve training

[43] The description of competence is consistent with the description in QC 1000.

auditors on the application of the relevant requirements, including conducting an audit with investor protection in mind.

The note to paragraph .07 of the final standard reinforces the need for auditors to have knowledge and proficiency in the requirements relevant to the company being audited and the related industry. Further, the auditor's responsibilities for understanding the company's business and consideration of materiality in planning and performing an audit are specifically addressed in other PCAOB auditing standards,[44] and we expect that these responsibilities would already be included in training on auditing standards.

### 4. Due Professional Care, Including Professional Skepticism

#### i. Due professional care

*See paragraphs .09 through .10 of the new standard in Appendix 1.*

We proposed to require the auditor to exercise due professional care in all matters related to the audit. The proposed standard stated that due professional care (i) concerns what the auditor does and how well the auditor does it, and (ii) means acting with reasonable care and diligence, exercising professional skepticism, acting with integrity, and complying with applicable professional and legal requirements. The proposed requirement was based on the existing requirement in AS 1015 to exercise due professional care.

The proposing release explained that exercising due professional care "in all matters related to the audit" would encompass all aspects of planning and performing an audit, including client acceptance and continuance procedures, and would extend to periods after the issuance of the auditor's report, such as completion of audit documentation,[45] reporting on Form AP, *Auditor Reporting of Certain Audit Participants*,[46] and procedures performed in connection with filings under the federal securities statutes.[47] We also proposed to retain language from existing standards related to an auditor's use of the work of other auditors, which emphasized that other auditors are responsible for performing their work with due professional care.[48]

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[44] *See* AS 2110 and AS 2105, *Consideration of Materiality in Planning and Performing an Audit.*

[45] *See* AS 1215.15 (as proposed to be amended).

[46] *See* PCAOB Rule 3211, *Auditor Reporting of Certain Audit Participants*.

[47] *See* AS 4101, *Responsibilities Regarding Filings Under Federal Securities Statutes*, which describes the auditor's responsibilities when the auditor's report is included in filings under federal securities statutes.

[48] *See Planning and Supervision of Audits Involving Other Auditors and Dividing Responsibility for the Audit with Another Accounting Firm*, PCAOB Rel. No. 2022-002 (June 21, 2022) (amendments

Some commenters acknowledged that due professional care is an important principle that should be retained in the final standard. Several commenters expressed support for requiring auditors to exercise due professional care "in all matters related to the audit."

Some commenters, primarily some firms, advocated for retaining certain contextual language from AS 1015.03-.04, including, for example, the description of due professional care in the 1932 legal treatise, *Cooley on Torts*.[49] These commenters expressed concern that without such language there may be a lack of transparency, or confusion among investors and other stakeholders, about the limitations of due professional care.

After considering comments, we are adopting the requirement to exercise due professional care as proposed. We continue to believe that the description of due professional care in the final standard is consistent with the description in AS 1015.03 (and the reference in the current standard to the legal treatise, *Cooley on Torts*), which uses the terms "reasonable care and diligence" and "good faith and integrity but not infallibility" to describe due care. As discussed in the proposal, we have retained explicit reference to "reasonable care and diligence," which we believe is well understood. We also believe that "good faith and integrity" means acting with "integrity." Our use of the term "integrity" aligns with its meaning established in EI 1000, which we are adopting in connection with the Quality Control rulemaking. EI 1000 codifies the concepts of integrity and objectivity, emphasizing that integrity includes being honest and candid, not knowingly or recklessly misrepresenting facts, and not subordinating judgment.[50] We believe that the terms used to describe due professional care are clear and should not cause confusion, as suggested by some commenters, because we have not changed the meaning of due professional care.

The proposed standard specified that, for engagement partners, due professional care also includes (i) appropriately assigning responsibilities to, and supervising, engagement team members; (ii) determining that the audit is properly planned and performed to obtain reasonable assurance; (iii) evaluating that significant findings or issues are appropriately addressed; (iv) determining that significant judgments and conclusions on which the auditor's report is based are appropriate and supported by sufficient appropriate audit evidence; and (v) determining that required communications under applicable professional and legal requirements have been made.

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approved by the SEC in Rel. No. 34-95488 (Aug. 12, 2022)), which amended AS 1015 to add this provision.

[49] The treatise states, among other things, that "no man, whether skilled or unskilled, undertakes that the task he assumes shall be performed successfully, and without fault or error; he undertakes for good faith and integrity, but not for infallibility, and he is liable to his employer for negligence, bad faith, or dishonesty, but not for losses consequent upon pure errors of judgment."

[50] *See also* PCAOB Rel. No. 2024-005.

The proposed clarifications of the engagement partner's responsibilities leveraged existing requirements for planning and performing an audit and for completing the corresponding audit documentation. For example, AS 1215 describes matters that are considered to be significant findings or issues in an audit and requires the auditor to document the significant findings or issues, including the actions taken to address them.[51] As part of the engagement partner's supervisory responsibilities under AS 1201, the proposal stated that the engagement partner would need to evaluate (in a timely manner) the significant findings and issues identified by the engagement team to ensure appropriate action was taken.[52]

Similarly, the proposal stated that significant judgments made by the engagement team, which AS 1220 specifically requires the EQR to review, also warrant the engagement partner's review. Because the engagement partner has primary responsibility for the engagement, they have primary responsibility for the significant judgments made during the engagement, notwithstanding any involvement in or responsibility for those judgments by firm personnel outside of the engagement team, such as members of the firm's national office. Accordingly, the "significant judgments made by the engagement team" include all of the significant judgments made during the engagement.[53] The proposed standard aligned the engagement partner's supervisory and review activities with existing auditor responsibilities.

A few commenters addressed the proposed requirement regarding the engagement partner's responsibilities for exercising due professional care. One commenter recommended separating the partner's responsibilities from the broader requirement to exercise due professional care. Another commenter expressed concern that, as presented, the responsibilities of the engagement partner could be viewed as a substitute for the broader responsibilities applicable to all auditors. This commenter suggested emphasizing in the final standard that for engagement partners, the responsibilities are in addition to those required for all auditors.

Several commenters also suggested clarifications to the proposed requirements. For example, one commenter suggested that the requirements be extended to team members performing supervisory activities. Another commenter pointed to potential inconsistencies with requirements of AS 1201 and AS 2101, noting that AS 1201 does not explicitly require the partner to assign activities to team members that adequately match their levels of competence and allows the partner to seek assistance from appropriate engagement team members in fulfilling responsibilities. One commenter recommended adding a footnote to AS 1220 to the discussion of significant judgments and conclusions.

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[51] *See* AS 1215.12.

[52] *See* AS 1201.05.

[53] *See Auditing Standard No.7 – Engagement Quality Review and Conforming Amendment to the Board's Interim Quality Controls Standards*, PCAOB Rel. No. 2009-004 (July 28, 2009), at 4 n.7.

In response to commenters, we have relocated the proposed engagement partner's responsibility for due professional care into a separate paragraph in the final standard, with certain clarifications. Specifically, we agree with commenters' views that the engagement partner is not required to directly assign responsibilities to all engagement team members (e.g., audit staff at other accounting firms involved in the audit). Nevertheless, consistent with AS 1015.06, the engagement partner is responsible for the appropriate assignment of tasks to, and supervision of, engagement team members. As such, the final standard states that the engagement partner's responsibility for due professional care includes "being responsible for the appropriate assignment of responsibilities to, and supervision of, engagement team members." This formulation acknowledges that in certain audit engagements, such as large, multi-tiered audits, the engagement partner may not be directly assigning work to engagement team members. Instead, other engagement team members performing supervisory activities may assist the engagement partner and inform engagement team members of their responsibilities.[54]

We believe that relocating the engagement partner's responsibility for due professional care into a separate paragraph helps draw a distinction between the responsibilities applicable to all auditors and those that are incremental for engagement partners. To clarify this further, we added "also" to the requirement in paragraph .10 to indicate that the engagement partner responsibilities for due professional care are in addition to those applicable to all auditors. We did not expand the applicability of the engagement partner responsibilities described in AS 1000 to other members of the engagement team performing supervisory activities because, as discussed above, the intent of this requirement is to focus the engagement partner on exercising due professional care as the person with the primary responsibility for the engagement and its performance. As suggested by one commenter, we added a footnote to the final standard referencing AS 1220 for the discussion of significant judgments and conclusions. We are adopting the remaining provisions of the requirement as proposed.

### ii. Description of professional skepticism

*See paragraph .11 of the new standard in Appendix 1.*

The proposed standard stated that exercising due professional care includes exercising professional skepticism in conducting an audit, and described professional skepticism as an attitude that includes a questioning mind and a critical assessment of information related to the audit. This requirement is based on the existing auditor responsibility to exercise professional skepticism in AS 1015. We emphasized in the proposal that application of professional skepticism extends beyond the information used as audit evidence, which is described in AS 1105.02 as the information "that is used by the auditor in arriving at conclusions on which the auditor's opinion is based." For example, by exercising professional skepticism in the preparation of Form AP, the auditor may become aware of inconsistencies in total audit hours

[54] *See* AS 1201.05.

reported by another accounting firm participating in the audit based on the level of work assigned to that accounting firm and take corrective action.

An investor-related group supported the proposed description of professional skepticism to include a critical assessment of information related to the audit. In contrast, a number of other commenters, mostly firms, expressed concern about the proposed change in the description of professional skepticism from a critical assessment of "audit evidence" to "information related to the audit," stating that this language is overly broad and its meaning unclear. Some of these commenters noted that, unlike with audit evidence, there is no established framework for auditors to assess information related to the audit and it is unclear what such an assessment would entail. Many of these commenters advocated for retaining the extant description of professional skepticism in AS 1015.07, which includes "a critical assessment of audit evidence."

Some commenters offered additional explanation or suggestions, for example:

- One commenter indicated they were unable to identify information, other than Form AP data, that would be considered "information related to the audit" that is not already part of "audit evidence." This commenter and another recommended specifically incorporating Form AP data into the requirement.

- One commenter indicated the proposed language could risk including information related to the audit that was never presented to the auditor. This commenter suggested retaining reference to "audit evidence" and including a reference to information obtained to comply with rules of the Board.

- Another commenter recommended retaining the reference to "audit evidence" because this concept is supplemented by the requirements in proposed paragraph .11 and by the overarching responsibility to exercise due professional care in relation to all matters related to the audit (including the preparation of Form AP).

Several commenters offered other views related to the description of professional skepticism. For example, one commenter stated that the difference between "critical assessment of information related to the audit" and "objective evaluation of evidence obtained in an audit" in proposed paragraph .11 is unclear. This commenter suggested combining proposed paragraphs .10 and .11 or providing further guidance, including guidance that is aligned with other standard setters. Another commenter questioned the assumption in the proposed standard that all auditors can exercise professional skepticism consistently for the duration of the audit, pointing to a lack of research.

After consideration of comments, we have revised the description of professional skepticism. The final standard describes professional skepticism as "an attitude that includes a questioning mind and a critical assessment of audit evidence and other information that is obtained to comply with PCAOB standards and rules." While we agree with commenters that

information related to the audit that is obtained by the auditor is generally audit evidence, we continue to believe that the exercise of professional skepticism in an audit extends beyond the evaluation of the sufficiency and appropriateness of audit evidence. Professional skepticism is an attitude held by the auditor throughout the audit process. For example, AS 2401, *Consideration of Fraud in a Financial Statement Audit*, provides that professional skepticism requires an ongoing questioning of whether the information and evidence obtained suggests that a material misstatement due to fraud has occurred.[55] The revised description in AS 1000 retains the extant reference to "critical assessment of audit evidence" but also, as suggested by one commenter, refers to information obtained by the auditor to comply with PCAOB standards and rules, such as information to complete Form AP. We believe that the revised description will provide auditors with a clear framework for exercising professional skepticism and aligns with the auditor's obligation to exercise due professional care, which applies to all matters related to the audit.

As suggested by one commenter, the final standard also combines in paragraph .11 the description of professional skepticism (proposed paragraph .10) with the description of what exercising professional skepticism entails (proposed paragraph .11) discussed below. We believe this unified paragraph will provide better context for the application of professional skepticism.

#### iii. Exercise of professional skepticism

*See paragraph .11 of the new standard in Appendix 1.*

The proposed standard described several factors involved in the exercise of professional skepticism, which were largely consistent with extant requirements. Under the proposed standard, the auditor's exercise of professional skepticism included:

- Objective evaluation of evidence obtained in an audit (including information that supports and corroborates management's assertions regarding the financial statements or internal control over financial reporting and information that contradicts such assertions), and consideration of the sufficiency and appropriateness (i.e., relevance and reliability) of that evidence;
- Remaining alert to conditions that may indicate possible misstatement due to error or fraud;
- Not relying on evidence that is less than persuasive;
- Not assuming that management is honest or dishonest; and

[55] *See* AS 2401.13.

- Consideration of potential bias on the part of management and the auditor.

Some commenters provided views on specific aspects of the factors involved in the auditor's exercise of professional skepticism. The comments and related responses are discussed in more detail below.

*Objectively evaluating evidence*. One commenter suggested requiring the auditor to search for contradictory evidence. Another commenter stated that the proposed description did not sufficiently address professional skepticism in obtaining audit evidence and instead focused only on evaluating the evidence. One commenter stated that the proposed description was unclear and suggested using more direct language, including requiring the auditor to be more neutral in the assessment (e.g., evaluating evidence that both supports assertions and evidence that does not).

The intent of paragraph .11a of AS 1000 is not to alter the responsibilities for obtaining and evaluating evidence addressed in AS 1105, but to remind auditors of their responsibility to exercise professional skepticism in connection with both obtaining and evaluating audit evidence. As discussed in the proposal, sufficient appropriate audit evidence is necessary to support the auditor's opinion. While primarily obtained from audit procedures performed during the audit, audit evidence may also include information obtained from other sources such as previous audits, and client acceptance or continuance procedures. The exercise of professional skepticism is particularly important in obtaining and evaluating audit evidence when responding to assessed risks of material misstatement, including fraud risks.

Audit evidence consists of both information that supports and corroborates management's assertions and information that contradicts such assertions.[56] The auditor's appropriate application of professional skepticism includes critically assessing this information and should result in procedures that are focused on obtaining evidence that is more relevant and reliable,[57] such as evidence obtained directly by the auditor and evidence obtained from independent, knowledgeable sources. Further, if audit evidence obtained from one source is inconsistent with audit evidence obtained from another, the auditor is required to perform the audit procedures necessary to resolve the matter and should determine the effect, if any, on other aspects of the audit.[58]

Professional skepticism is important in all aspects of the audit, particularly in those areas of the audit that involve significant management judgments or transactions outside the

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[56] *See* AS 1105.02. A new footnote has been added to AS 1000.11a, referring to AS 1105 for the discussion of management's assertions regarding the financial statements and internal control over financial reporting, and the proposed phrase "regarding the financial statements or internal control over financial reporting" has been deleted from paragraph .11a.

[57] *See* AS 1105.07-.08.

[58] *See* AS 1105.29.

normal course of business. It is ultimately the responsibility of each individual auditor to appropriately apply professional skepticism throughout the audit, including when (i) identifying and assessing risks of material misstatement, (ii) performing tests of controls and substantive procedures, and (iii) evaluating audit results. For example, a lack of professional skepticism in the risk assessment process could result in an auditor not identifying or assessing risks appropriately, which could impact the effectiveness of the audit.

*Remaining alert to conditions that may indicate possible misstatement due to fraud*. We did not receive significant comments in this area. As part of exercising professional skepticism, the auditor remains alert to conditions that may indicate possible misstatement due to error or fraud. This includes, for example, being alert to information that calls into question the reliability of documents and responses to inquiries the auditor plans to use as audit evidence. Such information could identify conditions that may indicate possible fraud or error in the financial statements. As discussed above, AS 2401 provides further requirements regarding potential fraud risk factors.

*Not relying on evidence that is less than persuasive*. One commenter stated that the proposed phrase "not rely" appears to be more restrictive than the existing phrase "not be satisfied with" in AS 1015.09 because the proposed phrase would preclude the auditor from placing any reliance on anything less than completely persuasive evidence, even in combination with other persuasive evidence.

The proposed phrase "not rely" was intended to convey that, consistent with AS 1015.09, exercising professional skepticism involves seeking evidence that is more persuasive rather than settling on evidence that may be less so. AS 1000 is not intended to address the sufficiency and appropriateness of evidence. To avoid confusion, the final standard retains the existing terminology from AS 1015 as "not being satisfied with evidence that is less than persuasive." The requirements for obtaining audit evidence, including evaluating its relevance and reliability, are discussed in AS 1105, which provides that the quantity of audit evidence needed is affected by both the risk of material misstatement and the quality of the evidence obtained (i.e., its relevance and reliability). To supplement evidence that is less relevant or obtained from a less reliable source, an auditor would need to gather additional evidence. The appropriate application of professional skepticism focuses the auditor on seeking the best evidence reasonably obtainable.

*Not assuming that management is honest or dishonest*. An investor-related group referenced certain views expressed in the 2000 report by the Public Oversight Board's Panel on Audit Effectiveness.[59] That report recommended that auditing standards require forensic-type fieldwork in which auditors would "modify the otherwise neutral concept of professional skepticism and presume the possibility of dishonesty at various levels of management, including

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[59] *See* Public Oversight Board, *The Panel on Audit Effectiveness Report and Recommendations* (Aug. 31, 2000).

collusion, override of internal control and falsification of documents."[60] We believe that establishing a presumption of management's dishonesty would have broader implications beyond the exercise of professional skepticism under this standard.

*Consideration of potential bias on the part of management and the auditor*. Several commenters expressed concern that the obligations related to consideration of the auditor's own bias were unclear or could be viewed as a requirement to seek contradictory evidence. Some of these commenters noted that consideration of auditor bias is inherent in the requirements for evaluating audit evidence under AS 1105 and suggested deleting the reference to "and the auditor" from proposed paragraph .11e. One commenter suggested aligning this concept with the approach used by the AICPA in their revised audit evidence standard. Two commenters also questioned the nature and extent of documentation necessary to demonstrate consideration of auditor bias. One investor-related group advocated for requiring the auditor to affirmatively consider the risk of bias, particularly confirmation bias, arising out of the financial relationship between management and the auditor.

We continue to believe that it is important to include reference to auditor bias in connection with exercising professional skepticism because certain conditions inherent in the audit environment create incentives and pressures that could impede the appropriate application of professional skepticism and allow unconscious bias to influence decisions. Examples of these incentives and pressures include avoiding significant conflicts with management, providing an unqualified audit opinion prior to the company's filing deadline, achieving high client satisfaction ratings, keeping audit costs low, or cross-selling other services.

As discussed in the proposal, it is important for the auditor, as part of exercising professional skepticism, to consider the impact of management bias and the auditor's own bias that could affect the auditor's judgments. For example, the tendency to seek confirming information can lead the auditor to seek audit evidence that is only consistent with management's explanations, or to favor conclusions that are consistent with the auditor's initial beliefs or conclusions reached in prior year audits. In exercising professional skepticism, the auditor could mitigate such potential bias by being aware of "confirmation bias," considering alternatives provided by others, and being aware of contradictory information.[61] Auditors and management may also have biases related to electronic information (e.g., a belief that electronic information is either always reliable or inherently prone to error). For example, a tendency to favor output generated from automated systems, even when contradictory information raises questions as to whether such output is reliable, illustrates a form of bias. Exercising professional skepticism, including critically assessing information related to the audit, helps the auditor address the effects of potential bias on professional judgment and decision-making. It is important to clarify, however, that the consideration of potential bias discussed

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[60] *Id.* at 88-89.

[61] For a discussion of confirmation bias, *see, e.g.*, Raymond S. Nickerson, *Confirmation Bias: A Ubiquitous Phenomenon in Many Guises*, 2 Review of General Psychology 175 (1998).

above does not change the auditor's responsibilities for evaluating contradictory evidence, as suggested by some commenters.

Finally, we are not adding new documentation requirements for demonstrating the auditor's exercise of professional skepticism beyond those addressed in AS 1215. Auditors can demonstrate that their work encompassed the exercise of professional skepticism by documenting the procedures performed and conclusions reached in accordance with AS 1215.

After consideration of the comments, we are adopting the provisions for exercising professional skepticism substantially as proposed, with the modifications discussed above.

### 5. Professional Judgment

*See paragraph .12 of the new standard in Appendix 1.*

Auditors exercise professional judgment throughout the audit, and existing standards refer to the use of professional judgment, but do not describe in detail what professional judgment means. The proposed standard provided that the auditor must exercise professional judgment and included a description of professional judgment. As discussed in the proposing release, auditors exercise professional judgment throughout the audit. For example, the auditor exercises professional judgment in:

- Determining the areas to be tested and the nature, timing, and extent of the tests to be performed;
- Interpreting the results of audit testing and evaluating audit evidence;
- Evaluating the reasonableness of accounting estimates in significant accounts and disclosures, based on information that could reasonably be expected to be available through the date of the auditor's report;[62]
- Determining if there are any CAMs in the audit of the financial statements;[63] and
- Determining the nature and extent of documentation to comply with documentation requirements.[64]

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[62] *See* AS 2501, *Auditing Accounting Estimates, Including Fair Value Measurements*, which discusses the auditor's responsibility to obtain sufficient appropriate evidence to determine whether accounting estimates in significant accounts and disclosures are properly accounted for and disclosed in the financial statements.

[63] *See* AS 3101 for requirements regarding CAMs.

[64] *See* AS 1215 for documentation requirements.

As proposed, professional judgment involved applying relevant training, knowledge, and experience to make informed decisions and reach well-reasoned conclusions about the courses of action that are appropriate in the circumstances such that the audit is planned and performed, and the report or reports are issued, in accordance with applicable professional and legal requirements.

Several commenters, primarily firms, expressed concern that the proposed description of professional judgment could be interpreted as imposing a new strict liability requirement. These commenters suggested removing the phrase "such that the audit is planned and performed, and the report or reports are issued, in accordance with applicable professional and legal requirements" in the description, noting that a deficiency in an auditor's compliance with applicable professional and legal requirements should not, by default, indicate a failure to exercise appropriate professional judgment. In the view of these commenters, this implication would be contrary to the established interpretation of an auditor's responsibilities, which recognizes that reasonable observers may disagree regarding whether applicable standards were complied with while agreeing that the matter in question was within the purview of the auditors' professional judgment and could result in hindsight challenges of auditors' judgments.

One commenter recommended that the description of professional judgment refer to "sound" judgment, consistent with the description used by the International Ethics Standards Board for Accountants ("IESBA").[65] Another commenter asked for clarification of the concept of "well-reasoned conclusions," noting potential differences with the definition of professional judgment established by other standard setters. Two commenters advocated for the establishment of a judgment framework by the Board. One commenter stated that they heard auditors express the need for more clarity about the degree of documentation necessary to demonstrate their reasoned judgment. Another commenter suggested adding the concept of materiality to the description of an auditor's exercise of judgment, based on the description of judgment in AS 2815.04 with regard to the auditor's opinion on financial statements.

The proposed phrase "such that the audit is planned and performed, and the report or reports are issued, in accordance with applicable professional and legal requirements" was meant to provide context to the application of professional judgment and was not intended to introduce a strict liability requirement. After considering the comments received, we removed this phrase in the final description of professional judgment. We continue to believe that it is important to clarify that the use of professional judgment does not allow for an arbitrary exercise of discretion. While conclusions could vary, auditors are required to apply relevant training, knowledge, and experience to make informed decisions and reach well-reasoned conclusions about the courses of action that are appropriate in the circumstances. Therefore,

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[65] *See* IESBA, *Handbook of the International Code of Ethics for Professional Accountants* (2023), Subsection 113 – Professional Competence and Due Care, at 113.1 A1 ("Serving clients and employing organizations with professional competence requires the exercise of sound judgment in applying professional knowledge and skill when undertaking professional activities.").

we added a note to paragraph .12 to clarify that professional judgment is applied in the context of conducting an audit with due professional care in accordance with applicable professional and legal requirements. We believe that this note properly frames the exercise of professional judgment without implying that a deficiency in an auditor's compliance with applicable professional and legal requirements would by default also indicate a failure to exercise appropriate professional judgment.

We did not change the description of professional judgment to include "sound judgment" as we believe that term is redundant with the phrase "well-reasoned." The phrase "well-reasoned," used in the context of an auditor exercising professional judgment and reaching conclusions, is clear because it refers to judgment made and conclusions reached that are based on logical thinking and an analysis of relevant information.

As discussed earlier, the auditor is required to exercise due professional care in all matters related to the audit. The concept of the auditor's exercise of professional judgment is rooted in conducting the audit with due professional care. Therefore, we are retaining the phrase "well-reasoned" as proposed. Regarding the degree of documentation related to professional judgment, the auditor is expected to comply with documentation requirements of AS 1215, which includes requirements for considering the nature and extent of documentation needed.

We believe that creating a "framework" for how auditors should exercise their professional judgment, as suggested by some commenters, would be beyond the scope of this project. We further believe it is better for auditors to adhere to overarching principles and standards that mandate the exercise of professional judgment in connection with conducting an audit with due professional care. This approach acknowledges the multifaceted nature of audits and allows auditors to exercise their professional judgment in the unique circumstances of each audit engagement.

## 6. Conducting an Audit

### i. Auditor and management responsibilities

*See paragraph .13 of the new standard in Appendix 1.*

We proposed to require the auditor to plan and perform the audit to obtain sufficient appropriate audit evidence to (a) obtain reasonable assurance about whether: (1) in an audit of financial statements, the financial statements are free of material misstatement, whether due to error or fraud, or (2) in an audit of ICFR, material weaknesses exist as of the date specified in management's assessment; and (b) provide the auditor with a reasonable basis for forming an opinion. This requirement was retained from AS 1001 and AS 1015 but expanded to cover an audit of ICFR. We also proposed to include a note to the requirement that clarified the distinction between the responsibilities of the auditor and those of management, and to expand those responsibilities to include an audit of ICFR. Specifically, the note stated that in an

audit of financial statements, the financial statements are management's responsibility and the auditor's responsibility is to express an opinion on the financial statements. In an audit of ICFR, management is responsible for maintaining effective ICFR and for assessing the effectiveness of ICFR, and the auditor's responsibility is to express an opinion on the effectiveness of the company's ICFR.

Several commenters discussed the importance of clearly distinguishing the responsibilities of the auditor from those of management and suggested retaining the corresponding language from AS 1001.02-.03. For example, one commenter observed that some investors may mistakenly believe that the auditor drafts the financial statements. In the view of this commenter, stating that management is "responsible" for the financial statements may be interpreted as a legal responsibility and does not explicitly convey that management prepares the financial statements.

We are retaining the requirement substantially as proposed. In response to commenters, we updated the language in the note to clarify that the financial statements, "including their preparation," are the responsibility of management and that management is responsible for "establishing and maintaining" effective ICFR.

#### ii. Reasonable assurance

*See paragraph.14 of the new standard in Appendix 1.*

We proposed to retain the concept of reasonable assurance from AS 1015. Specifically, the proposed standard stated that reasonable assurance is a high level of assurance and is obtained by reducing audit risk to an appropriately low level through the application of due professional care, including in obtaining sufficient appropriate audit evidence.[66] The auditor is able to obtain reasonable, but not absolute, assurance that (1) misstatements are detected that, individually or in combination, would result in material misstatement of the financial statements; and (2) in an audit of ICFR, material weaknesses are detected.

Commenters generally supported retaining the concept of reasonable assurance but provided views on its proposed description. A number of commenters, primarily firms, recommended that we retain certain statements from AS 1015.10-.13 (or similar language) that describe the limitations of an audit. These statements include:

- Absolute assurance is not attainable because of the nature of audit evidence and the characteristics of fraud. Therefore, an audit conducted in accordance with the

[66] *See* paragraph .03 of AS 1101, *Audit Risk*.

standards of the PCAOB may not detect a material weakness in internal control over financial reporting or a material misstatement to the financial statements.[67]

- Even with good faith and integrity, mistakes and errors in judgment can be made. …. [I]n the great majority of cases, the auditor has to rely on evidence that is persuasive rather than convincing.[68]

- Because of the characteristics of fraud, a properly planned and performed audit may not detect a material misstatement.[69]

- [T]he auditor is not an insurer and his or her report does not constitute a guarantee. Therefore, the subsequent discovery that either a material misstatement, whether from error or fraud, exists in the financial statements or a material weakness in internal control over financial reporting exists does not, in and of itself, evidence (a) failure to obtain reasonable assurance, (b) inadequate planning, performance, or judgment, (c) the absence of due professional care, or (d) a failure to comply with the standards of the PCAOB.[70]

A few of these commenters also pointed to the characterization of reasonable assurance in the standards of other standard setters (e.g., ISA 200).[71] These commenters generally expressed concern that without such language, the proposal would reduce transparency and contribute to the expectation gap among investors and other stakeholders regarding the nature of reasonable assurance (as compared to absolute assurance). For example, one commenter stated that the elimination of the existing clarifying language could also result in ambiguity as to whether a new level of assurance would be expected, beyond reasonable assurance but less than absolute assurance.

Some commenters offered other clarifications. For example, two commenters suggested retaining certain language from AS 1001.02, which states that the auditor has no responsibility

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67 *See* AS 1015.10.

68 *See* AS 1015.11.

69 *See* AS 1015.12.

70 *See* AS 1015.13.

71 Paragraph 13(m) of ISA 200 defines reasonable assurance as "in the context of an audit of financial statements, a high, but not absolute, level of assurance." Paragraph 5 of ISA 200 further describes that reasonable assurance "is obtained when the auditor has obtained sufficient appropriate audit evidence to reduce audit risk (that is, the risk that the auditor expresses an inappropriate opinion when the financial statements are materially misstated) to an acceptably low level. However, reasonable assurance is not an absolute level of assurance, because there are inherent limitations of an audit which result in most of the audit evidence on which the auditor draws conclusions and bases the auditor's opinion being persuasive rather than conclusive."

to plan and perform the audit to obtain reasonable assurance that misstatements, whether caused by errors or fraud, that are not material to the financial statements are detected. One of these commenters also acknowledged that identifying limitations on the auditor's responsibilities should not be the main focus of the standard. One commenter recommended that the final standard include guidance on determining whether audit risk is reduced to an appropriately low level, including a requirement to consider changes in technology, the nature and quality of an issuer's financial reporting system, relevant academic and other research, and any other factor that can reduce the risk of material misstatements or fraud.

As discussed further below, we are retaining the description of reasonable assurance as proposed with some modifications. The concept of "reasonable assurance" is not new. Reasonable assurance refers to the auditor's degree of satisfaction that the evidence obtained during the audit supports the assertions of the financial statements. It is a high level of assurance and is obtained by reducing audit risk to an appropriately low level (i.e., the risk that the auditor expresses an inappropriate audit opinion when the financial statements are materially misstated or in an audit of ICFR, when a material weakness exists) through applying due professional care, including obtaining sufficient appropriate audit evidence.[72] AS 1101 discusses audit risk and the relationships among the various components of audit risk in an audit of financial statements. We retained a reference to AS 1101 in the final standard and added the description of the term "audit risk." We believe that additional guidance on consideration of audit risk, as suggested by one commenter, is outside the scope of this standard. If additional guidance is necessary regarding the auditor's assessment of and response to the risks of material misstatement in an audit, it would be provided in connection with the Board's risk assessment standards.[73]

We did not change the meaning of reasonable assurance or the requirement to obtain reasonable assurance. In consideration of comments received, we emphasized in the final requirement that reasonable assurance is not absolute assurance. As observed by some commenters, absolute assurance is not attainable because of the nature of audit evidence (e.g., selective testing involving professional judgments[74] regarding the nature, timing, and extent of procedures to be performed; and inherent uncertainty of accounting estimates), and the characteristics of fraud (e.g., falsified company documentation). In many cases, the auditor has to rely on evidence that is persuasive rather than convincing. Because we did not change the meaning of reasonable assurance, we believe that further explanation of the difference between reasonable assurance and absolute assurance is not needed in the final standard.

We did not retain additional descriptions of the inherent limitations of an audit from AS 1015.10-.13. We believe that these matters are part of the differences between reasonable

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[72] *See* AS 1101.03-.04.

[73] *See, e.g.*, AS 1101, AS 2101, AS 2105, AS 2110, and AS 2301.

[74] Section III.B.5 discusses requirements for exercising professional judgment.

and absolute assurance discussed above or addressed elsewhere in PCAOB standards. Although a properly planned and performed audit may not detect a material misstatement because of the characteristics of fraud, that does not diminish the auditor's responsibility to plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement, whether due to error or fraud.

### iii. Compliance with applicable professional and legal requirements

*See paragraph.15 of the new standard in Appendix 1.*

We proposed to require that the auditor comply with applicable professional and legal requirements in conducting the audit. As discussed above in Section III.B.2, the term "applicable professional and legal requirements" was proposed to have the same meaning as defined in proposed QC 1000. Under existing provisions, auditors are required to comply with PCAOB standards and rules. The proposed requirement emphasized that the overall objective of the auditor is achieved by complying with more than just the standards of the PCAOB. This includes compliance with requirements of Section 10A of the Exchange Act related to illegal acts, related party transactions, and an evaluation of whether there is substantial doubt about the ability of the company to continue as a going concern.[75] The proposed requirement also stated that, in fulfilling these requirements, the auditor should keep in mind its role in protecting investors.

One commenter on this proposed paragraph stated that the term "applicable professional and legal requirements" appears to exceed the Board's authority, citing Sections 104 and 105 of Sarbanes-Oxley and urged that the Board replace it with "PCAOB rules and standards." Two other commenters noted that applicable professional and legal requirements could be read broadly as a wide range of laws and regulations that do not directly bear on the conduct of audit engagements. Another commenter recommended adding clarifying language in the release to state that although the auditor is expected to comply with applicable legal requirements, the auditor is not expected to have the expertise of a lawyer or to express opinions on matters of law.

We disagree with the commenter's assertions regarding the Board's authority, which extends beyond PCAOB rules and standards. For example, Section 105(c)(4) of Sarbanes-Oxley empowers the Board to sanction a registered firm and its associated persons for violations not only of PCAOB rules and standards but also violations of "the provisions of the securities laws relating to the preparation and issuance of audit reports and the obligations and liabilities of accountants with respect thereto, including the rules of the Commission issued under [the] Act[.]"

As discussed above, the final standard includes a definition of the term "applicable professional and legal requirements" rather than a reference to the definition in QC 1000. The

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[75] 15 U.S.C. § 78j-1.

definition that was proposed in the QC 1000 project has been modified in response to comments received in that rulemaking, to explicitly mention ethics laws and regulations. The definition was also refined to limit the breadth of the term, by clarifying that it encompasses statutory, regulatory, and other legal requirements beyond professional standards and other PCAOB rules "[t]o the extent related to the obligations and responsibilities of accountants or auditors in the conduct of engagements or in relation to the quality control system." We believe that further changes to this term in the final standard are not necessary.

As discussed above in Section III.B.3, we changed "expertise" to "proficiency" in the final description of competence in response to comments. While we do not expect auditors to have the expertise of a lawyer, we believe that understanding the company's business and being proficient in the rules and regulations relevant to the company under audit and the related industry is important.

Some commenters also stated that the requirement for auditors to "keep in mind their role in protecting investors" when fulfilling the requirement to comply with applicable professional and legal requirements was unclear, including how to apply such a requirement. As discussed in Section III.B.1 above, investor-related groups suggested including the language from the *Arthur Young opinion* to describe the auditor's responsibility. Other commenters suggested that the proposed reference to the auditor's role in protecting investors be deleted from the final requirement or reframed. One commenter pointed to research noting that encouraging auditors to adopt an investor perspective when making judgments may be detrimental to audit quality.[76]

After considering comments and for the reasons discussed above, we retained the requirement to comply with applicable professional and legal requirements. We removed the reference to "keep in mind their role in protecting investors" from the final standard based on changes made to paragraph .01 of the final standard. As discussed earlier, in connection with certain revisions made to the introductory paragraph of the final standard, we added a note to paragraph .01 to remind auditors that their obligation to protect investors is important when complying with all requirements of this and other PCAOB standards and rules.

#### iv. Relevant guidance

*See paragraph.15 of the new standard in Appendix 1.*

We also proposed a note to paragraph .15 stating that, as part of complying with all applicable professional and legal requirements in conducting the audit, the auditor is required to take into account relevant guidance applicable to the audit. The proposed requirement was

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[76] This commenter cited two research papers: (i) Altiero, Kang, and Peecher (2022) "show that auditors prompted to take an investor perspective are less likely to assess a misstatement as material" and (ii) Dong, Wang, and Chien (2022) "highlight that taking an investor perspective can decrease assessed risk of material misstatement." *See* additional discussion below in Section IV.C.3.i.

an extension of the existing requirement in AS 1001.11 that the auditor be aware of and consider auditing interpretations issued by the AICPA as of 2003, and adopted by the PCAOB and in effect. Under the proposal, relevant guidance included PCAOB auditing interpretations, Board-issued guidance, and releases that accompany the rules and standards of the Board.

Many commenters, mostly firms and firm-related groups, expressed concern that the proposed note is overly broad and unclear. For example, some commenters cited a lack of clarity as to (i) the scope of the Board-issued guidance including whether documents such as concept releases would be covered; (ii) the timeline in which the requirement would apply; (iii) the hierarchy of guidance and what types of guidance would be considered authoritative; and (iv) how to reconcile potentially conflicting information between proposing and final releases. These commenters generally suggested either deleting the note, codifying the relevant guidance to ensure consistent application, or specifying that relevant guidance includes releases accompanying "final" standards. Another commenter also suggested clarifying the meaning of "take into account," including defining the phrase in PCAOB Rule 3101.

A few commenters, including an investor-related group, recommended including relevant guidance within the standard rather than the accompanying release. Two commenters suggested that the Board consider restructuring guidance in a manner similar to the application and other explanatory material, as presented in the AICPA and IAASB standards. An investor-related group recommended a "codification" approach that would include placing all guidance, interpretations, releases, amendments, and rules in the same location.

After considering comments received, we have revised the note as follows:

- Replaced the reference to "relevant guidance" with "PCAOB auditing interpretations;" and
- Replaced a footnote describing the scope of the relevant guidance with a footnote describing the scope of PCAOB auditing interpretations.

The note in the final standard provides that, when complying with PCAOB standards, the auditor is required to also take into account PCAOB auditing interpretations applicable to the audit. As mentioned previously, this is an existing requirement that is being carried forward with modifications. In the final standard, PCAOB auditing interpretations refer to the PCAOB publications entitled "Auditing Interpretations" as currently in effect.[77] These interpretations were originally adopted by the Board in 2003 along with the interim standards. Since that time, certain of these auditing interpretations have been and continue to be revised or rescinded in connection with the other amendments to PCAOB standards. The requirement in the final standard, as it did previously, relates to the interpretations currently in effect.

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[77] PCAOB auditing interpretations do not include independence interpretations. The requirements to comply with independence interpretations are covered by PCAOB Rule 3500T, *Interim Ethics and Independence Standards*.

Apart from the PCAOB auditing interpretations referenced in paragraph .15, the PCAOB also supports the implementation of and compliance with its standards in many other ways, including providing guidance in rulemaking releases that accompany standards, amendments, or rules, or issuing staff guidance.[78] Although there is no requirement to follow these guidance documents, we continue to believe that it is important for auditors to pay attention to such guidance, if relevant, when conducting an audit in accordance with PCAOB standards because it may help the auditor understand and comply with complex provisions of those standards or rules. For example, staff guidance can help auditors better understand how the PCAOB intends to implement, inspect against, or enforce existing rules and standards.

The phrase "take into account" in the rule text is not new. It has been used previously in PCAOB standards in reference to information or matters that the auditor should think about or give attention to in performing an audit procedure or reaching a conclusion.[79] Accordingly, the results of the auditor's thinking on the relevant matters should be reflected in the performance and documentation of the respective audit procedure performed or conclusion reached.

Lastly, we did not consider the "codification" approach because it is out of scope for this project.

#### v. Audit documentation

*See paragraph.16 of the new standard in Appendix 1.*

We proposed to require the auditor to prepare audit documentation in accordance with AS 1215. This requirement was intended to emphasize the importance of adequate audit documentation to planning and performing the audit and to the supervision and review of work performed during the audit. Commenters did not express concerns with the documentation requirement, and we are adopting it as proposed.

#### vi. Auditor communications

*See paragraphs .17 through .20 of the new standard in Appendix 1.*

We proposed an explicit requirement for the auditor's report to contain (i) an expression of opinion on the financial statements, taken as a whole, or an assertion that an opinion cannot be expressed; and (ii) in an audit of internal control over financial reporting, an

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[78] PCAOB staff prepares guidance to assist in the implementation of PCAOB standards and rules. The typical legend on such guidance states that the document represents the views of PCAOB staff and not necessarily those of the Board, and that the document is not a rule, policy, or statement of the Board. PCAOB staff audit practice alerts are examples of staff guidance that highlight new, emerging, or otherwise noteworthy circumstances that may affect how auditors conduct audits under existing PCAOB standards.

[79] *See, e.g.*, AS 3101.12 and AS 2501.

expression of opinion on the effectiveness of the company's internal control over financial reporting or an assertion that an opinion cannot be expressed. Under the proposed standard, the auditor would be in a position to express an unqualified opinion only when the auditor has performed the audit in accordance with standards of the PCAOB and has obtained sufficient appropriate audit evidence to conclude that: (i) in an audit of financial statements, the financial statements, taken as a whole, are presented fairly, in all material respects, in conformity with the applicable financial reporting framework; and (ii) in an audit of internal control over financial reporting, the company maintained, in all material respects, effective internal control over financial reporting. The proposal also briefly addressed when circumstances require an auditor to express a qualified opinion, adverse opinion, or disclaimer of opinion and referred to AS 3105 and AS 2201 for a description of those circumstances. The proposed requirements were retained from AS 1001 with modifications to be consistent with provisions of AS 3101 and AS 2201.

One investor-related group requested that the required communications include CAMs, and that paragraph .17a of the proposed standard be revised to refer to CAMs "as a 'must contain' item in the auditor's report." The commenter was concerned with the low numbers of CAMs in auditor's reports and that auditors treat the determination of CAMs as "nearly a 'check the box' exercise." Another commenter suggested edits to proposed paragraphs .17 and .19 to align with existing requirements (e.g., adding the phrase "In an audit of financial statements" to paragraph .17a and moving the phrase "the company's" within paragraph .19).

We are adopting paragraphs .17-.19 substantially as proposed with some modifications. After considering the comments received, the reference to CAMs in a footnote has been moved to a note to paragraph .17 to emphasize the importance of CAMs. We did not make any additional changes to address concerns regarding CAMs. The proposal was not designed to address concerns about the frequency or informative quality of CAMs. Although we understand the importance of the concern raised by commenters, this is outside the scope of this project. We also revised paragraph .17a and paragraph .19 to incorporate commenters' suggestions described above. Additionally, we changed the phrase "modify the report" to "depart from an unqualified opinion" in paragraph .19 to align with other Board-issued standards that describe reports that include opinions other than an unqualified opinion.[80]

We proposed in paragraph .20 to require that the auditor communicate externally in accordance with applicable professional and legal requirements. This is an overarching requirement to communicate externally that is based on existing auditor communication requirements (e.g., AS 1301). We did not receive any comments on this requirement and are adopting it with slight modification. We changed "as required by" to "in accordance with" applicable professional and legal requirements to align with similar phrases used in other Board-issued standards.

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[80] *See, e.g.*, AS 3105.

## C. Amendments Related to AS 1000

Appendices 2 and 3 of this release present amendments to PCAOB standards related to AS 1000. The amendments we are adopting are described below.

### 1. Amendments to AS 2810 and Rescission of AS 2815 (Appendix 2)

We proposed to incorporate into AS 2810 the requirements of AS 2815 regarding the determination of whether the financial statements are presented fairly in conformity with the applicable financial reporting framework for a more logical presentation, and to rescind AS 2815. Currently, AS 2810 requires the auditor to evaluate whether the financial statements are presented fairly, in all material respects, in conformity with the applicable financial reporting framework, and AS 2815 describes the meaning of this evaluation. The proposed approach was intended to streamline these requirements into one standard and eliminate redundant or unnecessary language. A number of commenters commented on the proposed amendments to AS 2810. After considering the comments received, we are adopting amendments to AS 2810 with certain modifications discussed below.

#### i. Clarifying the meaning of "present fairly"

The discussion in the proposing release was designed to clarify the auditor's existing obligation to evaluate the fairness of the financial statements in conformity with the applicable financial reporting framework by stating that "present fairly," under extant PCAOB standards, is a concept that goes beyond mere technical compliance with the requirements of the applicable financial reporting framework.

Some commenters, primarily investor-related groups, supported clarifying the meaning of "present fairly" and provided additional suggestions on amendments to AS 2810. Two investor-related groups suggested that the Board consider going further and require auditors to focus on whether the financial statements are a fair presentation of the company's position rather than narrowly focusing on whether the company is following U.S. GAAP. One investor-related group suggested adding the word "and" immediately before the phrase "in conformity" to make it clear that there is an expectation that the financials are presented fairly, in all material respects *in addition to* conforming with the applicable financial reporting framework. Another group said that auditors should aid in disclosing and providing transparency around the sensitivity and accuracy of climate-related estimates and assumptions.

Other commenters, primarily firms and firm-related groups, viewed the proposed amendments as an expansion of auditors' existing responsibilities. Some commenters asserted that the statement in the proposal that the auditor's judgments concerning the fair presentation of the financial statements go beyond compliance with the applicable financial reporting framework may create a conflict between the auditor's judgment and management's judgment and introduce potential inconsistency in accounting treatment. Others expressed concern that under the proposal, auditors would expect the company to override the

requirements of an applicable financial reporting framework if the financial statements prepared in accordance with the framework did not fairly present the substance of the company's financial results.

Some commenters suggested retaining language from AS 2815.03 which states, "The independent auditor's judgment concerning the 'fairness' of the overall presentation of financial statements should be applied within the framework of generally accepted accounting principles. Without that framework, the auditor would have no uniform standard for judging the presentation of financial position, results of operations, and cash flows in financial statements." Other commenters suggested explicitly retaining the concept of professional judgment for evaluation of fair presentation.

Our proposed clarification of "present fairly" was not intended to change the auditor's existing responsibilities for the evaluation of whether the financial statements are presented fairly in conformity with the applicable financial reporting framework.

First, the amendments to AS 2810 clarify that "presents fairly" involves evaluating whether information in the financial statements is presented and classified appropriately and in a manner that is not misleading, and that this evaluation is made within the applicable financial reporting framework. Contrary to the views of some commenters, the amendments do not require auditors to expect that the company override or deviate from the requirements of the applicable financial reporting framework. Any override or deviation from the requirements of the applicable financial reporting framework would normally result in a departure from an unqualified opinion under PCAOB standards.[81] Further, the auditor is required to evaluate the risk of omitted, incomplete, or inaccurate disclosures as part of the auditor's risk assessment procedures.[82]

Second, the amendments acknowledge that applicable financial reporting frameworks recognize that additional disclosures may be needed to ensure fair presentation. For example, as noted above, the SEC requires by rule that a company provide further material information as necessary to make any required statements, in the light of the circumstances under which

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[81] *See* AS 3105. In addition, under SEC rules, a company's "[f]inancial statements filed with the Commission which are not prepared in accordance with generally accepted accounting principles will be presumed to be misleading or inaccurate, despite footnote or other disclosures, unless the Commission has otherwise provided." Regulation S-X Rule 4-01(a)(1), 17 C.F.R. § 210.4-01(a)(1). Paragraph (a) of that rule also provides that "the information required with respect to any statement shall be furnished as a minimum requirement to which shall be added such further material information as is necessary to make the required statements, in the light of the circumstances under which they are made, not misleading."

[82] *See, e.g.*, AS 2110.67, which requires the auditor, as part of the auditor's evaluation of fraud risk factors, to include evaluation of how fraud could be perpetrated or concealed by presenting incomplete or inaccurate disclosures or omitting disclosures that are necessary for the financial statements to be presented fairly in conformity with the applicable financial reporting framework.

they are made, not misleading.[83] This obligation is also consistent with the accounting standards issued by the FASB[84] and International Accounting Standards Board ("IASB").[85] Thus, when the auditor evaluates whether company transactions have been recorded and presented in conformity with the applicable financial reporting framework, the auditor may determine that additional company disclosures are needed to better reflect the substance of the transactions. Such evaluation is currently required under both AS 2810.31 and AS 2815.06, and the requirement is retained in the amendments to AS 2810.30A and .31.

In response to commenters, we are retaining, in the first note to AS 2810.30, the language of AS 2815.03, with some modifications. Specifically, we revised the reference to "generally accepted accounting principles" to "applicable financial reporting framework." We rephrased the sentence to emphasize that the "applicable financial reporting framework

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[83] *See* Regulation S-X Rule 4-01(a), 17 C.F.R. § 210.4-01(a).

[84] *See, e.g.*, FASB Accounting Standards Codification ("FASB ASC") paragraph 105-10-05-1, Generally Accepted Accounting Principles – Overall – Overview and Background ("Rules and interpretive releases of the Securities and Exchange Commission (SEC) under authority of federal securities laws are also sources of authoritative GAAP for SEC registrants."); FASB ASC paragraph 235-10-05-3, Presentation – Notes to Financial Statements – Overall - Overview and Background – Importance of Accounting Policies Disclosure ("The accounting policies of an entity are the specific accounting principles and the methods of applying those principles that are judged by the management of the entity to be the most appropriate in the circumstances to present fairly financial position, cash flows, and results of operations in accordance with generally accepted accounting principles (GAAP) and that, accordingly, have been adopted for preparing the financial statements.").

[85] *See, e.g.*, IASB International Accounting Standards ("IAS") 1, paragraph 15, Presentation of Financial Statements – Financial Statements – General features – Fair presentation and compliance with IFRSs ("Financial statements shall present fairly the financial position, financial performance and cash flows of an entity. Fair presentation requires the faithful representation of the effects of transactions, other events and conditions in accordance with the definitions and recognition criteria for assets, liabilities, income and expenses set out in the *Conceptual Framework for Financial Reporting (Conceptual Framework).* The application of IFRSs, with additional disclosure when necessary, is presumed to result in financial statements that achieve a fair presentation."); IAS 1, paragraphs 19-24, Presentation of Financial Statements – Financial Statements – General features – Fair presentation and compliance with IFRSs (describing financial reporting responsibilities in the "extremely rare circumstances in which management concludes that compliance with a requirement in an IFRS would be so misleading that it would conflict with the objective of financial statements set out in the *Conceptual Framework*"); IAS 8, paragraph 10, Accounting Policies, Changes in Accounting Estimates and Errors ("In the absence of an IFRS that specifically applies to a transaction, other event or condition, management shall use its judgement in developing and applying an accounting policy that results in information that is: (a) relevant to the economic decision-making needs of users; and (b) reliable, in that the financial statements: (i) represent faithfully the financial position, financial performance and cash flows of the entity; (ii) reflect the economic substance of transactions, other events and conditions, and not merely the legal form; (iii) are neutral, ie free from bias; (iv) are prudent; and (v) are complete in all material respects.").

provides the basis for the auditor's judgment regarding the presentation of financial position, results of operations, cash flows, and disclosures in financial statements." We also agree with commenters that the auditor's evaluation of fairness of presentation of the financial statements is an exercise of professional judgment in the context of an applicable financial reporting framework. The first note to AS 2810.30 refers to the auditor's judgment when evaluating the fairness of the overall presentation of financial statements.

We have also added a new footnote to paragraph .30A, as discussed below, referencing SEC Rule 4-01(a) that describes the company's obligation regarding additional information that may need to be disclosed in the financial statements so that the financial statements are not misleading.

**ii. References to SEC Rule 12b-20**

The proposed amendment to AS 2810.30 included a new footnote 17A that referred to a company's responsibility pursuant to SEC Rule 12b-20 under the Exchange Act, 17 C.F.R. § 240.12b-20 ("SEC Rule 12b-20"). That rule requires the company to disclose "such further material information, if any, as may be necessary to make the required statements, in the light of the circumstances under which they are made not misleading."

Most commenters who addressed the proposed citation to SEC Rule 12b-20 expressed concern with it. While one investor-related group recommended relocating the proposed footnote to the body of the amendments due to its significance, other commenters suggested removing the reference to SEC Rule 12b-20, with some commenters objecting primarily because the rule pertains to companies' disclosures within or beyond the financial statements. Some commenters emphasized that disclosures beyond the financial statements are the responsibility of companies rather than of auditors. Many expressed concerns that referring to the rule might be viewed as expanding the auditor's responsibilities, or would conflict with the auditor's responsibilities described in AS 3101.08e.[86] One of these commenters suggested citing SEC Rule 4-01(a)(1) instead, because that rule relates specifically to financial statements, upon which the auditor expresses an opinion.

After considering the comments received, we are deleting proposed footnote 17A with the reference to SEC Rule 12b-20 from the final amendment to AS 2810.30 because that rule reflects a company's responsibilities for information beyond as well as within the financial statements.[87] Instead, we are retaining the existing note to that paragraph requiring that the

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[86] AS 3101.08e requires that the auditor's report include an opinion that the financial statements present fairly, in all material respects, the financial position of the company, results of operations, and cash flows in conformity with the applicable financial reporting framework, and that the opinion identify the applicable financial reporting framework.

[87] The auditor's responsibility for other information outside of the financial statements is specified in AS 2710, *Other Information in Documents Containing Audited Financial Statements*.

auditor look to the requirements of the SEC for the company under audit with respect to the accounting principles applicable to that company. The requirements of the SEC for the company under audit are included in SEC Rule 4-01(a), which we reference in a new footnote to paragraph .30A, to remind auditors of the company's obligation regarding additional information that may need to be disclosed in the financial statements so that the financial statements are not misleading.

### iii. Other clarifications to proposed AS 2810.30A

We proposed a new paragraph AS 2810.30A based on the extant requirement from AS 2815.04, using language consistent with other PCAOB standards. Specifically, we:

- Combined the concepts in AS 2815.04a – b regarding acceptability and appropriateness of accounting principles and presented them in AS 2810.30Ab;
- Retained the concepts from AS 2815.04c – d regarding informativeness of information presented in the financial statements and presented them as a new AS 2810.30Aa; and
- Retained the concepts from AS 2815.04e regarding transactions presented in the financial statements within a range of acceptable limits as a new AS 2810.30Ac and an amendment to AS 2810.31.

Several commenters expressed concern about not retaining the reference to the "within a range of acceptable limits" from AS 2815 and suggested (i) retaining this phrase in AS 2810.30A or (ii) revising proposed 2810.30A to include a footnote referencing AS 2110 or a note describing the relationship between AS 2810.30A and AS 2110 and adding "in all material respects" to AS 2810.30Ac. Another commenter suggested defining "a reasonable investor" used in AS 2810.30Aa. One commenter encouraged the Board to provide guidance on the use of the term "informative" in AS 2810.30A because it could be widely interpreted and applied in practice.

In addition, several commenters suggested including or clarifying certain terminology or concepts used in the proposed new paragraph, AS 2810.30A. Suggestions included:

- Referencing the importance of exercising professional judgment when evaluating the requirements specified in AS 2810.30A; and
- Clarifying that (i) "financial statements" include all notes to the statements and all related schedules;[88] and (ii) "disclosures" used in AS 2810.30A means

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88 *See* Regulation S-X Rule 1-01(b), 17 C.F.R. 210.1-01(b).

"accompanying notes," not other information included in management discussion and analysis ("MD&A") and other disclosures included in the annual report.

After considering the comments received, we are retaining proposed paragraph .30A with modifications discussed below.

The final AS 2810.30A requires an auditor, when evaluating whether the financial statements (including the accompanying notes) present fairly the financial position, results of operations, and cash flows, in all material respects, in conformity with the applicable financial reporting framework, to evaluate whether:

a. The financial statements are informative of matters that may affect their use, understanding, and interpretation; and the information in the financial statements is presented and classified appropriately and in a manner that is not misleading;

b. The accounting principles selected and applied by the company's management are appropriate in the circumstances; and

c. Company transactions and relevant events and conditions are appropriately recognized, measured, and disclosed in the financial statements.

We added "(including the accompanying notes)" in AS 2810.30A to clarify that financial statements include the accompanying notes, to match the description in AS 2810.31 of financial statements as "financial statements (including the accompanying notes)." Because we use "disclosures" as an interchangeable term with "notes" or "accompanying notes" throughout PCAOB standards, it is unnecessary to further clarify the terms in AS 2810.30A. We also did not add a reference to professional judgment in AS 2810.30A, but as discussed above we have revised the first note to AS 2810.30 to clarify that the auditor uses professional judgment when evaluating the fairness of financial statements.

The term "informative" is in AS 2815.04c, which refers to AS 2810.31, which in turn provides additional considerations for evaluation of information disclosed in the financial statements (e.g., consideration of the form, arrangement, and the amount of detail given). To clarify this further, we retained in the final standard language from AS 2815.04c stating that the information in the financial statements is presented appropriately, in a manner that is "informative of matters that may affect their use, understanding and interpretation" and not misleading. We removed the reference to "reasonable investor" from AS 2810.30A because it was limiting and did not consider a broader population of financial statement users (e.g., creditors). We also believe that introducing "reasonable investor" in AS 2810.30A may create confusion by implying that an analysis is needed that is distinct from determining if the financial statements are presented fairly in conformity with the applicable financial reporting framework.

Finally, we do not believe it is necessary to retain a reference to "within a range of acceptable limits" in AS 2810.30A. The standard is clear that evaluation of fairness is based on auditor judgment and that the concept of materiality is inherent in that judgment, which involves the consideration of qualitative as well as quantitative factors. The combination of these considerations should be clear that not every transaction or account is evaluated to arrive at the conclusion that the company's financial statements, taken as a whole, are presented fairly, in all material respects.

**iv. Other clarifications to proposed AS 2810.31**

We proposed to revise the note to AS 2810.31 by (i) removing the first sentence that describes the requirements from AS 3105 (i.e., inadequate disclosures) and instead adding a reference to AS 3105.24-.27 in paragraph .31, and (ii) adding an extant requirement from AS 2815.06 for the auditor to also evaluate whether the substance of transaction or events differs materially from their form, but changing it from "should consider" to "should evaluate."

Several commenters suggested, in addition to retaining the requirement from AS 2815.06, to also retain a provision from AS 2815.06 that states "generally accepted accounting principles recognize the importance of reporting transactions and events in accordance with their substance." Some commenters suggested not changing the "should consider" requirement from extant AS 2815.06 to "should evaluate" when evaluating a transaction in substance over form. Additionally, some commenters recommended removing or relocating the note in AS 2810.31 to proposed AS 2810.30A for better context.

Two investor-related groups suggested providing guidance on AS 2810.31 by adding the existing concept of what the auditors are required to do (per AS 2815.04c) when the applicable financial reporting framework does not provide guidance (e.g., financial statements and accompanying notes do not disclose the necessary information required), or what considerations should be given by auditors in evaluating fair presentation of financial statements in accordance with proposed AS 2810.30.

After considering the comments received, rather than amending the existing note to AS 2810.31, we have removed the note in its entirety. We believe that a separate requirement to evaluate whether the substance of transactions differs from their form is unnecessary in light of the requirement in new AS 2810.30Aa. As discussed above, AS 2810.30Aa requires auditors to evaluate "whether the financial statements are informative of matters that may affect their use, understanding, and interpretation;" and the information in the financial statements is presented and classified appropriately and in a manner that is not misleading. This evaluation includes determining whether additional disclosures are necessary to reflect, for example, the substance of the company's transactions. The auditor's evaluation of whether company transactions have been recorded and presented in conformity with the applicable financial reporting framework includes the determination of whether additional disclosures are needed in the financial statements.

We also believe that AS 2810.31 and the amendments are comprehensive and clear, and thus no additional guidance is warranted. For example, under US GAAP and IFRS, management has a range of conforming choices in selecting classifications and measurements of revenue recognition, segment reporting, and fair value measurement. The auditor is responsible for evaluating whether the disclosures reflect the choices made by management and are not misleading to investors and other financial statement users.

### 2. Amendments Related to Engagement Partner Responsibilities for Supervision (Appendix 2)

#### i. Seeking assistance from other engagement team members

AS 1201 and AS 2101 establish the engagement partner's responsibility for the engagement and its performance, including planning, supervision, and review. We proposed to amend the existing requirements in AS 1201 and AS 2101 to clarify that even when the engagement partner seeks assistance from other engagement team members, the engagement partner retains the primary responsibility for the engagement and its performance. One commenter strongly supported these amendments, and we are adopting them as proposed.

The final notes added to AS 1201 and AS 2101 clarify that while an engagement partner may seek assistance on specific tasks from other engagement team members, they continue to retain the primary responsibility for supervising, reviewing, and ensuring the quality of the work performed in the audit. In other words, the work of other engagement team members does not replace or reduce the engagement partner's responsibility for the engagement and its performance.

#### ii. Timing of review

We also proposed a requirement to clarify that the review and evaluation by the engagement partner (and as applicable by other engagement team members performing supervisory activities) of work performed by engagement team members, as described in AS 1201.05c, must be completed prior to the report release date. These amendments did not receive any comment and are being adopted as proposed.

#### iii. Workpaper review

We proposed to amend AS 1201 to clarify the extent of the planning, supervisory, review, and documentation activities to be performed by the engagement partner by aligning those activities with existing auditor responsibilities under AS 1015 because we believe that the engagement partner's review of audit documentation is an important part of supervision. These amendments were intended to reaffirm the engagement partner's supervisory and review responsibilities in the context of exercising due professional care.[89] Specifically, we proposed to

[89] *See* AS 1000.10 discussed above.

add a note stating that notwithstanding assistance from other engagement team members performing supervisory activities, the engagement partner is required to review sufficient documentation to determine that (i) the engagement was performed as planned; (ii) significant judgments were appropriate and significant findings and issues, along with matters brought to the engagement partner's attention pursuant to AS 1201.05b, were appropriately addressed; (iii) the conclusions expressed in the auditor's report are appropriate and supported by sufficient appropriate evidence; and (iv) matters requiring communication under applicable professional and legal requirements are appropriately identified and communicated. The proposed note also provided that the engagement partner's review includes review of documentation of significant findings or issues[90] and review of documentation that is also subject to review by the EQR, citing the provisions of AS 1220 that specifically require the EQR to review certain documentation.[91]

One commenter stated that the proposed amendments were overly prescriptive and should allow more flexibility regarding the engagement partner's review and sign-off. Another commenter recommended clarifying how due professional care in AS 1201 relates to the engagement partner's responsibilities in AS 1000. This commenter further recommended better aligning AS 1201 with proposed AS 1000.09, including the interplay between Note 2 of AS 1201.05, which has specific workpaper review requirements by the engagement partner, while AS 1201.04 also allows the engagement partner to seek assistance from other engagement team members.

After considering the comments received, we are adopting amendments to AS 1201 substantially as proposed. We believe that the amendments clarify the engagement partner's existing obligations for supervision and review. As the engagement team member with primary responsibility for the engagement, the engagement partner must review, at minimum, sufficient documentation of specific audit areas that are deemed important to support the auditor's opinion. Without reviewing sufficient documentation in these areas, the engagement partner would not be able to demonstrate that the engagement partner has the primary responsibility for the audit.

One commenter asserted that the proposed requirement that the "engagement partner's review should include review of documentation … subject to review by the engagement quality reviewer" could be interpreted to require the engagement partner to review all documentation reviewed by the EQR, beyond what is required in AS 1220.10 or .15. Another commenter expressed concern about the proposed note stating that in multi-tiered audits, other audit partners, not only the engagement partner, should retain the ability to review all documentation subject to EQR review. This commenter suggested not linking engagement partner review requirements to documentation subject to review by EQR.

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90 *See* AS 1215.12.

91 *See* AS 1220.09-.10 and .14-.15.

In response to the commenters, we have clarified the final requirement by changing the phrase "review of documentation subject to review by the engagement quality reviewer" to "review of documentation required to be reviewed by the engagement quality reviewer pursuant to the requirements of paragraphs .09-.10 and .14-.15 of AS 1220 …." This revision further clarifies that we expect the engagement partner to review the documentation that the engagement quality reviewer is required to review in order to comply with those provisions of AS 1220, rather than all of the documentation that the engagement quality reviewer may have actually reviewed. We believe that the documentation of significant judgments made and conclusions reached by the engagement team that is required to be reviewed by the EQR provides important information to the engagement partner. This is true for all engagements, including multi-location and multi-tiered engagements. The extent of documentation reviewed by the EQR and, under the final amendment, by the engagement partner, will depend on the facts and circumstances of the particular engagement. Further, the requirement for the engagement partner to review documentation required to be reviewed by the EQR does not preclude other engagement team members performing supervisory activities to also review this documentation.

Several commenters further expressed concerns that the proposed amendments create an incorrect perception that the responsibility for all phases of the audit resides with the engagement partner only without any consideration given to the responsibility of the firm or other engagement team members. One of these commenters further suggested including a statement that the engagement partner should tailor the extent of their supervision based on a variety of factors as described in AS 1201.06. AS 1201.05 specifically addresses the responsibilities of the engagement partner relating to supervision of engagement team members, and we do not think it is necessary to change these requirements to address the responsibilities of others.

One commenter stated that the engagement partner's review of documentation to determine that the engagement was performed as planned may be construed as expanding the partner review requirements beyond AS 1215.12c because the review of documentation only relates to "results of auditing procedures that indicate a need for significant modification of planned auditing procedures." We do not believe that Note 2 of AS 1201.05 expands the engagement partner's responsibilities. AS 2101.03 states that the engagement partner is responsible for planning the audit and that the engagement partner retains primary responsibility for the engagement and its performance. In addition, the documentation requirements under AS 1215 are not limited to the significant findings and issues described in AS 1215.12 and there are other documentation requirements outside of documenting specific matters.

Another commenter further suggested that we define "sufficient documentation" used in proposed Note 2 of AS 1201.05. We do not believe this is necessary. What is sufficient will depend on the facts and circumstances of the particular engagement under review. The amount of documentation that the engagement partner would review will vary depending on

the associated risk involved in the audit area and the nature of the work performed that the engagement partner reviews. We further clarified this point, by changing "sufficient documentation to determine" to "documentation sufficient to determine" in the final amendment. This change is designed to better connect the concept of sufficiency with the matters that the engagement partner will determine.

We also proposed other amendments to AS 1201 and AS 2101 to conform to the adoption of AS 1000. These technical and clarifying amendments included replacing references to titles of existing standards with the title of the new standard and updating cross-referenced terminology and paragraph citations. We are adopting these other amendments as proposed as no comments were received.

### 3. Amendments Related to Documentation (Appendix 2)

We proposed several amendments to AS 1215 discussed in more detail below. Commenters generally supported the proposed amendments to AS 1215. Some commenters provided specific comments related to (i) documentation completion date and (ii) specific audit documentation and timing for documentation review. These are discussed in more detail below.

#### i. Documentation completion date

Audit documentation is the written record of the basis for the auditor's conclusions that provides the support for the auditor's representations, whether those representations are contained in the auditor's report or otherwise. Audit documentation also facilitates the planning, performance, and supervision of the engagement, and is the basis for the review of the quality of the work because it provides the reviewer with written documentation of the evidence supporting the auditor's significant conclusions.[92] Under existing standards, a complete and final set of audit documentation is required to be assembled for retention as of a date not more than 45 days after the report release date, known as the documentation completion date.[93] We proposed to accelerate the documentation completion date by reducing the maximum period from 45 days to 14 days.

Many commenters who addressed the amendment generally supported it or agreed that the proposed acceleration of the documentation completion date would be appropriate or result in increased audit quality. Two commenters further stated that the shorter period of 14 days would not cause significant changes at most firms.

Several commenters raised concerns over the acceleration of the documentation completion date. One commenter stated that the acceleration would likely lead to more audit

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92 *See* AS 1215.02.

93 *See* AS 1215.15.

quality issues due to the increasingly more complex financial accounting, reporting, and auditing landscape requiring more time as well as the current talent crisis. Another commenter stated that 14 days is too short to handle any unforeseen consequences (e.g., technology interruptions). Another commenter questioned whether acceleration of documentation will (i) have any meaningful impact on PCAOB inspection timelines and operating efficiencies and (ii) be workable for smaller firms, who may not have the technology to implement this change.

Two commenters, both investor-related groups, recommended further shortening the documentation completion date to two days because an earlier PCAOB inspection would benefit investors. These two investor-related groups and another commenter questioned why 14 days is a more appropriate timeframe. Focusing on challenges that smaller firms may face in implementing the acceleration, and the diversity across global network firms in documentation archive systems, several commenters recommended a phased implementation approach or extending the implementation over a longer period (e.g., two-year period).

The proposal also sought comment, in light of the proposed 14-day documentation completion date, on whether firms would have difficulty, when filing Form AP within 35 days of the audit report being filed, complying with AS 1215.16. That paragraph of AS 1215 prohibits the deletion or discarding of audit documentation after the documentation completion date but permits the addition of documentation under certain conditions. Two firms stated that they did not foresee significant difficulties in complying with AS 1215.16 with additional costs, while another firm indicated some technological and process challenges. Two commenters recommended making both due dates (i.e., documentation completion date and Form AP due date) the same.

After considering the comments received, we are adopting the accelerated documentation completion date of 14 days as proposed with modification to the effective date for certain firms discussed below. The 14-day timeline strikes a good balance of meeting the objectives of this amendment (e.g., enhance investor protection by enabling the Board to begin the inspection process sooner after the completion of an audit) while still allowing a two-week period (14 calendar days) to assemble audit documentation for retention (i.e., archive audit documentation). As echoed by some commenters, we believe that the accelerated documentation period will not require a significant change for many firms. In our view, the changes to the archiving period (i.e., 14 days) are necessary to focus auditors on assembling a complete set of audit documentation that is high-quality and without documentation errors or omissions in a timely manner. We believe that a delay in assembling the audit documentation increases the potential for omissions to occur.

Further, shortening the archiving period also reduces the window of opportunity for improper alteration of audit documentation and increases the quality of documentation because recalling and describing audit procedures long after the work was actually performed can be difficult.

In accordance with AS 1215, the auditor must have completed all necessary auditing procedures and obtained sufficient evidence to support the representations in the auditor's report before the report release date.[94] The presence of complex financial accounting, reporting, or auditing matters should not have a bearing on the archiving period as the effects of such matters on the audit should be addressed before the report release date (i.e., before the 14 days to assemble the audit documentation). Under existing AS 1215.16 auditors are allowed to add documentation after the documentation completion date, if needed.[95] While we understand that in practice some firms use a short archiving period, we believe that an archiving period of two days, as suggested by investor-related groups, may be too short to handle any unforeseen consequences (e.g., technology interruptions) and could result in inadvertent non-compliance.

We also continue to believe that the accelerated documentation completion date of 14 days is still appropriate even when considering the Form AP deadline of 35 days. We acknowledge that in most situations, firms currently have 35 days to file Form AP,[96] and a firm must document the computation of total audit hours and include that computation in the files.[97] If the actual hours become available after the documentation completion date but before the Form AP filing, the auditor is required under provisions of AS 1215 to add that information to the audit documentation after the documentation completion date.[98] The instructions to Form AP also provide that firms may use a reasonable method to estimate audit hours when actual hours have not been reported or are otherwise unavailable.[99]

We acknowledge that certain firms may have less technologically advanced systems in place and may need more time to implement new processes to comply with the accelerated documentation completion date requirement. Therefore, as discussed in more detail in Section VI, the effective dates for this requirement allow a phased-in approach for smaller firms to comply with the 14-day documentation completion date. This approach addresses implementation challenges that some commenters suggested smaller firms may face.

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94 *See* AS 1215.15 (as amended).

95 *See* AS 1215.16.

96 Form AP has a filing deadline of 35 days after the date the auditor's report is first included in a document filed with the SEC, or 10 days after the auditor's report is first included in a document filed with the SEC for a registration statement under the Securities Act of 1933. PCAOB Rule 3211(b).

97 *See Improving the Transparency of Audits: Rules to Require Disclosure of Certain Audit Participants on a New PCAOB Form and Related Amendments to Auditing Standards*, PCAOB Rel. No. 2015-008 (Dec. 15, 2015).

98 *See* AS 1215.16.

99 *See* Instructions to Form AP, *Part IV – Responsibility for the Audit is Not Divided*.

### ii. Specific audit documentation and timing of review

We also proposed to emphasize that audit documentation must clearly demonstrate who performed the work, who reviewed the work, and the date of such review.[100] In order for an engagement partner to conclude that the audit evidence obtained is sufficient and appropriate to support the opinion expressed in the auditor's report,[101] the audit work is required to be reviewed prior to the report release date. Therefore, we also proposed to amend AS 1215.15 to clarify that, before the report release date, the engagement partner and other engagement team members performing supervisory activities have completed their reviews of audit documentation.

One commenter raised a concern that the amendments may result in lower quality documentation and an increase in late filings, providing an example of when a significant issue emerged closer to the issuer's filing deadline, because additional time to complete and review the relevant documentation would be needed. Another commenter suggested further clarifying whether the engagement partner and other supervisors must ensure that all review notes have been sufficiently addressed prior to the report release date.

We are adopting the amendments to AS 1215 as proposed. The requirement for the engagement partner and other supervisors to review relevant audit documentation prior to the report release date is a clarification of existing requirements in AS 1215 and AS 2101. As discussed earlier, since the auditor's report is dated no earlier than the date on which the auditor has obtained sufficient appropriate evidence to support the auditor's opinion,[102] the auditor must have completed all necessary auditing procedures, including documentation to support the work performed that is reviewed by the engagement partner and other reviewers, on or before the auditor's report date, in all cases. The engagement partner and other supervisors should refer to existing requirements in AS 1215.07, in determining the sufficiency of audit documentation. Several factors to consider include nature of the audit procedure, risk of material misstatement associated with the assertion, and extent of judgment required in performing the work and evaluating the results (i.e., accounting estimates require greater judgment and commensurately more extensive documentation).[103]

Lastly, in relation to proposed amendments in AS 1215.06 and .06A, one commenter agreed with the addition of paragraph .06A but suggested removing the phrase of "who performed the work, the person or persons who reviewed the work, and the date of such review" in AS 1215.06 because the same phrase is already included in AS 1215.06Ab. We did not make changes to the final amendments to AS 1215.06 and .06A. The addition of the phrase

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100 *See* AS 1215.06.

101 *See* AS 2810.02.

102 *See* paragraph .01 of AS 3110, *Dating of the Independent Auditor's Report*.

103 *See* AS 1215.07.

in paragraph .06 is an intentional clarification, rather than duplication, of what the audit documentation is required to demonstrate. The requirement in paragraph .06, is different, and relates to the sufficiency of documentation needed to meet the experienced auditor threshold.

We also proposed other amendments to AS 1215 to conform to AS 1000. These technical and clarifying amendments included replacing references to titles of existing standards with the title of the new standard and updating cross-referenced terminology and paragraph citations. We did not receive any comments relating to other amendments to AS 1215 and are adopting those as proposed.

### 4. Other Amendments (Appendix 3)

In connection with the adoption of AS 1000, the Board is also adopting other amendments to several PCAOB standards to conform with AS 1000, amendments to AS 2810, and rescission of AS 2815. These amendments include superseding the foundational auditing standards.

The other changes being adopted include replacing references to titles of existing standards with the title of the final standard and updating cross-referenced terminology and paragraph citations. See Appendix 3 for these other amendments.

The proposed amendments that received comments are discussed in more detail below.

#### i. Amendments to AS 2710, *Other Information in Documents Containing Audited Financial Statements*

AS 2710.05 refers to differences in the auditor's judgment or opinion. We proposed to amend that standard in two ways, by clarifying that the difference of judgment or opinion is "between the auditor and the client," and by adding a footnote clarifying the meaning of "judgment." One commenter suggested replacing "the client" with "management" to be consistent with other PCAOB standards. Although in this release we are adopting other amendments that refer to the management and audit committee of the company under audit rather than to the auditor's "client," we are not making this change throughout the auditing standards because such a sweeping change is outside the scope of this project and may not be warranted in each instance, and thus could create confusion. Because "client" is used in AS 2710 throughout the standard, we are retaining the use of that term in the existing standard and in the amendment, and thus are adopting the amendments to AS 2710.05 as proposed.

#### ii. Amendments to AS 3101, *The Auditor's Report on an Audit of Financial Statements When the Auditor Expresses an Unqualified Opinion*

We proposed to move certain language in paragraph .01 of AS 3101 to AS 1000. We also proposed to move footnote 2 that describes the term "taken as a whole" to paragraph .02 of AS 3101. Two commenters on the proposed amendments to AS 3101 suggested amending

paragraph .11 and paragraph .14, primarily due to the declining number of CAMs disclosed by firms. Other commenters suggested adding language about the meaning of reasonable assurance means and the limitation of the audit in the auditor's report (paragraph .09 and Appendix B). We did not make these changes suggested by commenters because they are outside the scope of this project.

One commenter expressed concern that the meaning of "taken as a whole" was changed because a footnote was added to AS 3101.02. As discussed above, we did not change the meaning of "taken as a whole" by moving the existing footnote to another paragraph. We are therefore adopting the amendments as proposed.

### iii. Amendments to AS 4105, *Reviews of Interim Financial Information*

We proposed to replace references to titles of existing standards with the title of the final standard and update cross-referenced terms and paragraph citations in paragraphs .01 and .07. Three commenters noted that the amendments are appropriate. One commenter suggested adding "to the extent those standards are relevant" in AS 4105.01 when referencing AS 1000 because interim reviews are not required to provide reasonable assurance. We believe this addition is not necessary because the amendment refers only to compliance with independence and ethics requirements, competence, and exercise of due professional care, which are fundamental to any audit, review, or attestation engagements under the PCAOB standards. All of these concepts are relevant to AS 4105 without exception. We are adopting the amendments as proposed.

### iv. Amendments to Attestation Standards

We proposed to replace references to titles of existing standards with the title of the final standard and update cross-referenced terms and paragraph citations. One commenter on these amendments stated that they are appropriate. Another commenter offered suggestions to (i) limit the references to AS 1000 in attestation standards because the general principles and responsibilities in AS 1000 should be specifically tailored to attestation engagements to be operable, (ii) retain paragraph .41 of AT Section 101, *Attest Engagements* a reference to *Cooley on Torts*, which was removed, and (iii) change the reference in footnote 9A of Attestation Standard No. 2, *Review Engagements Regarding Exemption Reports of Brokers and Dealers*, as "review" engagement as opposed to "examination" engagement. We note that the references to AS 1000 have been tailored to the attestation standards. We are not retaining the reference to the 1932 treatise *Cooley on Torts* because, as we explained when we proposed AS 1000, that reference is unnecessary and AS 1000 explains the concept of due professional care in plain language without changing its meaning.[104] We are revising the footnote of AT No. 2 to refer to a "review" engagement. Otherwise, we are adopting the amendments as proposed.

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[104] *See* PCAOB Rel. No. 2023-001, at 22.

# IV. ECONOMIC ANALYSIS

We are mindful of the economic impacts of our standard setting. This section describes the economic baseline, need, and expected economic impacts of the final standard and related amendments, as well as alternative approaches considered by the Board. Due to data limitations, the economic analysis is generally qualitative in nature.

We sought and received comments on the economic analysis in the proposing release.[105] A majority of the commenters expressed views related to the economic analysis, and they generally agreed with the need for the standard. Some commenters suggested that the use of certain proposed language or certain proposed clarifications could result in potential confusion or expansion of auditors' responsibilities or that the proposed removal of certain extant explanatory language could reduce transparency regarding the meaning of the general principles and responsibilities and exacerbate an audit expectation gap. Some commenters suggested that the economic analysis should more carefully consider potential costs or unintended consequences associated with certain key provisions. These comments are addressed below. One commenter asserted that costs that have not been analyzed, quantitatively or qualitatively, include costs to firms from new legal duties and auditor responsibilities. The commenters did not provide data to support their concerns about potential costs and unintended consequences. Their views were based on interpretations that the Board's proposal would make broader changes. However, we believe the economic analysis is appropriate and consistent with the limited scope of changes the rulemaking requires. Commenters generally agreed that accelerating the documentation completion date is feasible for firms and beneficial to investors, although some commenters noted potential costs or questioned the expected benefits. One commenter suggested potential unintended consequences associated with clarifying engagement partner responsibilities. Three commenters referenced additional academic research for our consideration. These comments are addressed below.

We have considered all of the comments received and have developed an economic analysis below that includes these considerations and evaluates the expected benefits and costs of the final standard and related amendments, discusses potential unintended consequences, and facilitates comparison to alternative actions considered. Specific input is discussed where relevant in the analysis that follows.

## A. Baseline

Section II of this release describes important components of the baseline against which the economic impacts of the standard can be considered, including an overview of existing

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[105] *See id.* at 55-57.

requirements. In the following subsections, we discuss additional matters that inform our understanding of the baseline for each of the changes.

### 1. Modernization of the Foundational Standards

Section II provides an overview of existing requirements of the auditing standards that describe the general principles and responsibilities of the auditor in conducting an audit in accordance with the standards of the PCAOB (i.e., foundational standards). The general principles and responsibilities addressed by the foundational standards are described in Section III.B and include reasonable assurance, due professional care, professional skepticism, independence, competence, and professional judgment.

The foundational standards are required to be followed in every audit conducted in accordance with PCAOB standards. The general principles and responsibilities in the foundational standards are reflected in firm methodologies, commercially published guidance, and other technical tools. Although there may be circumstances where some auditors' understanding of the general principles and responsibilities is made more difficult than necessary by how the foundational standards are organized and written, we do not have evidence that auditors are systematically confused about the meaning of the general principles and responsibilities or that the foundational standards are insufficient to support high-quality audits, when applied appropriately.

One commenter suggested there is no evidence that audit personnel are unclear or uncertain about the meaning of the proposed requirements. An investor-related group noted that the proposed standard was consistent with the extant standards.

The views expressed by the commenters align with our belief that the core general principles and responsibilities encompassed by the foundational standards are well-established and sound. While the foundational standards are currently spread across four standards (i.e., AS 1001, AS 1005, AS 1010, AS 1015), contain some extraneous restrictive language, and do not emphasize the investor protection obligation as prominently as desired, applied appropriately, they are sufficient to support high-quality audits.

### 2. Clarification of Engagement Partner Responsibilities

Under PCAOB standards, engagement partners are responsible for the engagement and its performance, including the proper planning and supervision of the engagement and its compliance with PCAOB standards. While engagement partners are permitted to seek assistance from other team members performing supervisory activities, engagement partners are responsible for proper supervision of the engagement and have primary responsibility for the engagement.

As discussed in the proposal, the staff reviewed firms' available methodology documentation to obtain an understanding of firms' policies and practices for engagement

partner review.[106] A number of larger firms have developed specific guidance, checklists, and other tools to facilitate the engagement partner's review. For example, some firms mandate the use of tools that specify workpapers or topics that engagement partners are required to review directly. These tools require the engagement partner to document their review. Conversely, similar policies of some smaller firms are designed to be applied at a higher level and are not as specific about the required review.[107] We did not receive comments that provided additional information addressing the baseline for engagement partner review.

### 3. Accelerating the Documentation Completion Date

The auditor is required to complete all necessary auditing procedures, review those procedures, and obtain sufficient appropriate audit evidence prior to the report release date. Auditors may need some time after the report release date to assemble the final audit file and complete the audit documentation. The PCAOB standard on audit documentation currently requires completion of documentation within 45 days after the report release date.

When PCAOB inspection staff select issuer audits for inspection, PCAOB notice of inspection and access to firm audit documentation generally do not occur until after the documentation completion date. After an inspection is complete, the Board issues a report on the inspection, and a portion of each report is made available to investors and the public on the PCAOB's website.

As discussed in the proposal, the staff reviewed firms' stated archiving policies and firms' archiving practices to obtain an understanding of firms' policies and practices for completing audit documentation.[108] We found a wide range of archiving periods among firms, from the full 45-day period to a much shorter period. In addition, PCAOB staff has observed that certain firms require audit documentation to be archive-ready upon completion of interim audit procedures. The PCAOB established the 45-day period in 2004[109] when firms relied more on paper documentation and needed time to copy, collate, finalize, and file workpapers. PCAOB staff has observed that most firms today have electronic audit tools and audit software that either make those tasks unnecessary or enable the tasks to be performed much faster.

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106 *See id.* at 36.

107 The observations in this paragraph are based on the staff's review of the policies of U.S. global network firms ("GNFs") and U.S. non-affiliate firms ("NAFs"). GNFs are the member firms of the six global accounting firm networks (BDO International Ltd., Deloitte Touche Tohmatsu Ltd., Ernst & Young Global Ltd., Grant Thornton International Ltd., KPMG International Ltd., and PricewaterhouseCoopers International Ltd.). NAFs are both U.S. and non-U.S. accounting firms registered with the Board that are not GNFs. Some of the NAFs belong to international networks.

108 *See* PCAOB Rel. No. 2023-001, at 37.

109 *See Audit Documentation and Amendment to Interim Auditing Standards*, PCAOB Rel. No. 2004-006 (June 9, 2004), at 5.

Some U.S. GNFs require engagement teams to archive audit documentation within 10 days after the report release date. Other firms require engagement teams to archive audit documentation within longer periods (ranging from 30 to 45 days after the report release date). Of the firms with policies that allow longer periods, certain of them express expectations to complete documentation within a much shorter period.

All GNFs have established global policies for archiving to be used by their respective non-U.S. affiliate firms. The global policies generally allow for completion of documentation not more than 45 days after the report release date. The global policies of certain GNFs specify a documentation completion date within 14 days after the report release date, or sooner when required by local laws or regulations. In addition to the global policies, certain non-U.S. affiliates of GNFs have local policies requiring documentation completion dates earlier than their respective global policies. Examples observed through the PCAOB's 2022 inspections include non-U.S. affiliates that have local policies specifying completion of documentation by deadlines such as 2 days, 7 days, 10 days, 14 days, and 30 days after the report release date. Additionally, even among certain non-U.S. affiliates that have stated policies of 45 days after the report release date, their documentation systems require completion of documentation within 15 to 40 days (depending on the firm). Generally, non-U.S. affiliates of GNFs use electronic audit documentation systems for documentation and archiving.

The archiving policies of NAFs generally specify a documentation completion date of 45 days after the report release date. PCAOB staff has observed certain NAFs annually inspected by the PCAOB that, in practice, typically archive documentation within 40 days of the report release date. In addition, PCAOB staff has noted that certain other NAFs generally complete their documentation at the end of the full 45-day archiving period. While most NAFs use electronic audit documentation systems, PCAOB staff is aware that some smaller firms still use paper-based workpapers.

We did not receive comments specific to the baseline for the documentation completion date, including additional information on firms' current archiving policies and practices.

## B. Need

The changes introduced in the final standard are part of the Board's effort to continuously improve and update PCAOB standards. In practice, PCAOB standards are used by auditors, who are responsible for applying the general principles and responsibilities of the foundational standards. Investors and other stakeholders may also rely on the foundational standards (directly or indirectly) to establish expectations about auditor responsibilities.

## 1. Problem to be Addressed

### i. Modernization of the foundational standards

We identified three potential concerns about the foundational standards: (i) compliance with the standards; (ii) soundness of the general principles and responsibilities; and (iii) clarity of the standards. The next three subsections explain that we do not see a need to make changes to the standards based on compliance with the standards or soundness of the general principles and responsibilities, but we do see a need to make changes to modernize and enhance the clarity of the foundational standards.

#### a. Compliance with the foundational standards

In some instances, auditors have not performed audits in compliance with the foundational standards. For example, for the years 2018-2022, the PCAOB issued almost two dozen enforcement orders that described the violation of at least one of the foundational standards. One commenter, an academic, noted research that suggests that audit failures often relate to basic areas of auditor responsibility, such as failure to gather sufficient appropriate audit evidence, failure to exercise due professional care, or insufficient professional skepticism.[110] The commenter added that contributing factors to the noted failures appear to be auditor disincentives to be skeptical[111] or high auditor workloads.[112] For example, research indicates that professional skepticism could be affected by priorities such as engagement budgets rather than investor protection.[113] The commenter also suggested that persistent audit deficiencies, despite PCAOB inspection and enforcement efforts, highlight the importance of auditors' understanding of and compliance with foundational auditing principles.[114] The views expressed by the commenter seem to align with our understanding of auditors' adherence to

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[110] *See, e.g.*, Mark S. Beasley, Joseph V. Carcello, Dana R. Hermanson, and Terry L. Neal, *An Analysis of Alleged Auditor Deficiencies in SEC Fraud Investigations: 1998-2010* (commissioned by Center for Audit Quality) (May 2013).

[111] *See, e.g.*, Joseph F. Brazel, Scott B. Jackson, Tammie J. Schaefer, and Bryan W. Stewart, *The Outcome Effect and Professional Skepticism*, 91 The Accounting Review 1577 (2016) and Joseph F. Brazel, Christine Gimbar, Eldar M. Maksymov, and Tammie J. Shaefer, *The Outcome Effect and Professional Skepticism: A Replication and a Failed Attempt at Mitigation*, 31 Behavioral Research in Accounting 135 (2019).

[112] *See, e.g.*, Julie S. Persellin, Jaime J. Schmidt, Scott D. Vandervelde, and Michael S. Wilkins, *Auditor Perceptions of Audit Workloads, Audit Quality, and Job Satisfaction*, 33 Accounting Horizons 95 (2019).

[113] *See, e.g.*, Brazel et al., *The Outcome Effect and Professional Skepticism* and Brazel et al., *The Outcome Effect and Professional Skepticism: A Replication and a Failed Attempt at Mitigation*.

[114] *See, e.g.*, Ashna L. Prasad and John C. Webster, *What Are the Trends in PCAOB Inspections and the Reported Audit Deficiencies?* 37 Journal of Accounting, Auditing & Finance 523 (2022).

the foundational standards and our assessment of the need to modernize and clarify those standards, including a reaffirmation of the auditor's obligation to protect investors.

### b. Soundness of the general principles and responsibilities

The foundational standards address the general principles and responsibilities of reasonable assurance, due professional care, professional skepticism, independence, competence, and professional judgment. These principles and responsibilities are interconnected. For example, due professional care requires the auditor to exercise professional skepticism, including a questioning mind and a critical assessment of audit evidence. Audit procedures performed with due professional care allow the auditor to obtain reasonable assurance about whether the financial statements are free of material misstatement. Reasonable assurance is achieved, in part, by the exercise of professional judgment, which involves the auditor making decisions based on applying relevant training, knowledge, and experience. There is ample published research that studies alternative versions of these general principles and responsibilities. We summarize here several papers that demonstrate an ongoing debate regarding alternatives.

As noted in the proposal,[115] academic research regarding professional skepticism provides a model that identifies two components – skeptical judgment and skeptical action – that are necessary for the effective exercise of professional skepticism.[116] In a synthesis of literature on professional skepticism, researchers conclude that professional skepticism is foundational to the performance of a high-quality audit, and they note that academic research tends to focus on skeptical judgment while PCAOB inspections tend to focus on skeptical action.[117] When accountability to regulators is an incentive based on principles, research suggests that auditors may exhibit more skeptical judgment.[118] When accountability is based on a checklist mentality of following a set of strictly specific requirements, research suggests that auditors may engage in cognitive processing that reduces skeptical judgment.[119] On the other

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115 *See* PCAOB Rel. No. 2023-001, at 39.

116 *See* Mark W. Nelson, *A Model and Literature Review of Professional Skepticism in Auditing*, 28 Auditing: A Journal of Practice & Theory 1, 5 (2009).

117 *See* R. Kathy Hurtt, Helen Brown-Liburd, Christine E. Earley, and Ganesh Krishnamoorthy, *Research on Auditor Professional Skepticism: Literature Synthesis and Opportunities for Future Research*, 32 Auditing: A Journal of Practice & Theory 45, 47 (2013). According to the authors, "Skeptical judgment occurs when an auditor recognizes that a potential issue may exist and that more work or effort is necessary. Skeptical action occurs when an auditor changes his/her behavior based on the skeptical judgment. Both skeptical judgment and skeptical action are essential to the audit, with skeptical judgment being a necessary condition for skeptical action."

118 *See* Hurtt, et al., *Research on Auditor* 62.

119 *See* M. David Piercey, *Documentation Requirements and Quantified versus Qualitative Audit Risk Assessments*, 30 Auditing: A Journal of Practice & Theory 223, 242-43 (2011).

hand, a principles-only approach to standards may provide insufficient guidance to support the exercise of judgment.[120] Overall, therefore, there is a spectrum of possible approaches to audit regulation that lies between excessively vague principles and excessively specific requirements. In practice, effective auditing standards may fit into the middle of that spectrum by emphasizing core principles while including some specific requirements to help support skeptical judgment and skeptical action.[121] One commenter, an academic, noted that research on rules- versus principles-based requirements for independence and ethics suggests that a combination of rules and principles is likely to be the most effective approach.[122]

One commenter referenced several academic papers and highlighted pragmatic challenges and costs auditors face when applying the concept of professional skepticism.[123] The commenter reported that past economic research finds violations of professional skepticism underlying audit deficiencies.[124] The commenter also reported that lack of professional skepticism by auditors regarding frauds of the early 2000s generated academic literature on models of professional skepticism,[125] a scale to measure professional skepticism traits,[126] and interventions designed to help increase professional skepticism.[127] Moreover, the commenter

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[120] *See, e.g.*, SEC, *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* (July 25, 2003).

[121] *See, e.g.*, AS 1210, *Using the Work of an Auditor-Engaged Specialist*.

[122] *See, e.g.*, Terri L. Herron and David L. Gilbertson, *Ethical Principles vs. Ethical Rules: The Moderating Effect of Moral Development on Audit Independence Judgments*, 14 Business Ethics Quarterly 499 (2004) and Bryan K. Church, J. Gregory Jenkins, and Jonathan D. Stanley, *Auditor Independence in the United States: Cornerstone of the Profession or Thorn in Our Side?* 32 Accounting Horizons 145 (2018).

[123] *See, e.g.*, Brazel et al., *The Outcome Effect*; Ashleigh L. Bakke, Elizabeth N. Cowle, Stephen P. Rowe, and Michael S. Wilkins, *How Do Audit Firms Treat Partners Who Issue Adverse Internal Control Opinions?* Available at SSRN: https://papers.ssrn.com/sol3/papers.cfm?abstract_id=4383557 (2023); Richard C. Hatfield, Scott B. Jackson, and Scott D. Vandervelde, *The Effects of Prior Auditor Involvement and Client Pressure on Proposed Audit Adjustments*, 23 Behavioral Research in Accounting 117 (2011); and Sandra Waller Shelton, *The Effect of Experience on the Use of Irrelevant Evidence in Auditor Judgment*, 74 The Accounting Review 217 (1999).

[124] *See, e.g.*, Mark S. Beasley, Joseph V. Carcello, and Dana R. Hermanson, *Top 10 Audit Deficiencies*, Journal of Accountancy 63 (2001).

[125] *See, e.g.*, Mark W. Nelson, *A Model and Literature Review of Professional Skepticism in Auditing*, 28 Auditing: A Journal of Practice & Theory 1 (2009).

[126] *See, e.g.*, R. Kathy Hurtt, *Development of a Scale to Measure Professional Skepticism*, 29 Auditing: A Journal of Practice & Theory 149 (2010).

[127] *See, e.g.*, Jessica Maree Cross, Robyn Moroney, and Soon-Yeow Phang, *Is it All in the Mind(Fulness)? An Exploratory Study Assessing the Impact of Mindfulness on Professional Skepticism*, 37 Accounting Horizons 25 (2023).

reported that an area of academic psychology research asserts that skeptical behavior is a personality trait that may require a counter-dispositional change in mindset.[128] (We note that this research does not specifically study professional skepticism as a general principle or responsibility in auditing.) In contrast, another commenter reported that academic research highlights the merits of focusing on both obtaining and evaluating information as a pragmatic approach in the exercise of professional skepticism.[129]

These comments suggest that efforts by firms, such as training and on-the-job-coaching, may be needed regarding professional skepticism, but do not suggest that professional skepticism as a general principle and responsibility of auditors is flawed. In addition, the views shared by these commenters underscore the need for a well-defined standard that sets forth the requirements of due professional care and professional skepticism, which is discussed further in Section IV.B.1.i.c below.

As noted in the proposal, research also offers insights on the appropriate and expected levels of assurance for investors and other users of financial statements.[130] One accounting firm referenced a literature review that notes the audit expectation gap has existed for many years and describes it as a phenomenon in which the expectations of beneficiaries of audited financial statements exceed what auditors can reasonably be expected to accomplish.[131] Early research on the audit expectation gap concludes that the majority of investors prefer absolute assurance that financial statements are free of material misstatement, in contrast to the profession's standard that an audit should provide reasonable assurance.[132] Similarly, a more

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128 *See, e.g.*, Lewis R. Goldberg, *The Structure of Phenotypic Personality Traits*, 48 American Psychologist 26 (1993); Paul E. Bebbington, Orla McBride, Craig Steel, Elizabeth Kuipers, Mirjana Radovanovic, Traolach Brugha, Rachel Jenkins, Howard I. Meltzer, and Daniel Freeman, *The Structure of Paranoia in the General Population*, 202 The British Journal of Psychiatry 419 (2013); and Ryan Hamilton, Kathleen D. Vohs, Anne-Laure Sellier, and Tom Meyvis, *Being of Two Minds: Switching Mindsets Exhausts Self-Regulatory Resources*, 115 Organizational Behavior and Human Decision Processes 13 (2011).

129 *See, e.g.*, Jonathan H. Grenier, *Encouraging Professional Skepticism in the Industry Specialization Era*, 142 Journal of Business Ethics 241 (2017) and Noel Harding and Ken T. Trotman, *The Effect of Partner Communications of Fraud Likelihood and Skeptical Orientation on Auditors' Professional Skepticism*, 36 Auditing: A Journal of Practice & Theory 111 (2017).

130 *See* PCAOB Rel. No. 2023-001, at 39.

131 *See* Reiner Quick, *The Audit Expectation Gap: A Review of the Academic Literature*, 94 Maandblad voor Accountancy en Bedrijfseconomie 5 (2020).

132 *See, e.g.*, Marc J. Epstein and Marshall A. Geiger, *Investor Views of Audit Assurance: Recent Evidence of the Expectation Gap*, 177 Journal of Accountancy 60, 64 (1994).

recent multi-country study finds that survey respondents appear to expect much more than reasonable assurance from auditors in order to prevent fraud and company failure.[133]

We believe this cross-section of research, either noted in the proposal or by commenters, aligns with our decision to maintain the core general principles and responsibilities of the foundational standards. The synthesis research supports professional skepticism as foundational to the performance of effective audits. Likewise, the research on audit assurance supports the principle of reasonable assurance as an appropriate level of assurance based on the underlying benefits and costs of an audit engagement.[134] As explained in Section III.B.6, absolute assurance is not attainable because of the nature of audit evidence and the characteristics of fraud. As described in this release, AS 1000 clarifies the general principles and responsibilities without substantially modifying the general principles and responsibilities. Moreover, we do not anticipate that the final standard and related amendments will markedly influence the current audit expectation gap since we are preserving the core concepts while making marginal adjustments to reaffirm the auditor's obligation to protect investors.

### c. Clarity of the foundational standards

As discussed in the proposal, some current features of the foundational standards do not support the most efficient use of the standards.[135] The general principles and responsibilities are currently spread across four standards, which were not developed originally as a cohesive whole. Their current organization continues to reflect their origin as separate requirements that were not drafted to be read together. In addition, the foundational standards contain language that was used in the AICPA's former standards but is outdated and inconsistent for audits conducted today under the standards of the PCAOB. This could undermine users' understanding of the general responsibilities of the auditor for audits conducted in accordance with PCAOB standards. The foundational standards also do not conform to the structure of Board-issued standards, which may hinder an auditor's navigation of the requirements. Finally, the foundational standards do not reflect developments in the auditing environment since their adoption in 2003, including the PCAOB's adoption of standards and rules, such as standards on audit documentation and engagement supervision, and this lack of consistency or alignment may draw attention away from the general principles and responsibilities.

Overall, these current features of the foundational standards may reduce efficient use of the standards by requiring more time and attention than necessary to read, understand, and apply the standards and may lead to inconsistent application, potential misinterpretation, and

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133 *See* Association of Chartered Certified Accountants, *Closing the Expectation Gap in Audit* (May 2019) ("ACCA Report").

134 *See, e.g.*, Ernest L. Hicks, *Materiality*, 2 Journal of Accounting Research 158 (1964).

135 *See* PCAOB Rel. No. 2023-001, at 40.

ineffective regulatory intervention. Clarity of auditing standards requires effective communication through features such as relevant language, consistency with Board-issued standards and rules, and well-organized presentation, which appear throughout PCAOB and SEC rulemaking initiatives.

Several firms and a firm-related group acknowledged that modernization efforts to streamline and clarify the foundational standards will enhance users' awareness and understanding of the auditor's responsibilities.

### (1) Characteristics of modernized auditing standards

Academic research identifies three characteristics of effective disclosure documents that align well with the features of modernized auditing standards: simplicity,[136] salience,[137] and standardization.[138] Simplicity can be achieved with an auditing standard that eliminates language that is outdated and inconsistent. Salience can be achieved with an auditing standard that emphasizes requirements while including explanations in the Board's release rather than the rule text and that incorporates the latest developments in the auditing environment, including the adoption of Board-issued standards and rules. Standardization can be achieved with an auditing standard that is well-organized, with general principles and responsibilities presented in a single standard that is structured similar to other standards.

In addition, we are aware of other regulatory initiatives that emphasize clear, well-organized writing as characteristics of effective communication with stakeholders. Two examples of other regulatory initiatives are the SEC Plain English Disclosure rule[139] for issuers' prospectuses, and the Plain Writing Act of 2010[140] for government communications with the public. The purpose of the Plain English Disclosure rule was to make financial and business information available to investors in a form they could read and understand, and the rule

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136 *See, e.g.*, R.E. Nisbett and L. Ross, *Human Inference: Strategies and Shortcomings of Social Judgment* (1980) (finding that individuals have limited cognitive resources to absorb and process information).

137 *See, e.g.*, Daniel Kahneman, *Thinking, Fast and Slow* (2013) (suggesting that individuals who focus their limited cognitive resources on a subset of information are able to give more weight to the subset when making decisions).

138 *See, e.g.*, Jeffrey R. Kling, Sendhil Mullainathan, Eldar Shafir, Lee C. Vermeulen, and Marian V. Wrobel, *Comparison Friction: Experimental Evidence from Medicare Drug Plans*, 127 The Quarterly Journal of Economics 199 (2012) (finding that standardized information better enables individuals to assess tradeoffs and make coherent, rational decisions).

139 *Plain English Disclosure*, SEC Rel. No. 33-7497 (Oct. 1, 1998).

140 *Plain Writing Act of 2010*, Public Law 111-274.

includes specific guidance for clear, concise language.[141] The purpose of the Plain Writing Act was to improve the effectiveness and accountability of federal agencies to the public by promoting clear communication that the public can understand and use, and the statute defines plain writing as writing that is clear, concise, and well-organized, and that follows other best practices appropriate to the subject and the intended audience.[142] While neither the Plain English Disclosure rule nor the Plain Writing Act imposes obligations on the PCAOB, their overall objective to promote effective communication for efficiency of stakeholders' understanding is aligned with the objectives of and approach to our modernization of the foundational standards.

We did not receive comments that provided additional information regarding characteristics of modernized auditing standards.

### (2) Useability of modernized auditing standards

As summarized in Section IV.A.1, we continue to believe that auditors generally understand their responsibilities under the foundational standards. Nonetheless, there could be certain circumstances where some auditors' understanding of the general principles and responsibilities is made more difficult than necessary by the current language and organization of the foundational standards. New entrants, for example, may need to spend more time navigating and distilling the extant general principles and responsibilities than they would with more modernized language and organization. These new entrants may include accounting students seeking to enter the auditing profession. They may also include auditors who are experienced in applying other auditing or attestation standards, such as those of the AICPA for entities other than issuers, but who are seeking to perform an audit under PCAOB standards for the first time and who need to confirm their responsibilities under PCAOB rules.

In addition, the current language and organization of the foundational standards could impede investors' abilities to form accurate expectations about auditor responsibilities under PCAOB standards. Investors form expectations from a number of sources, including potentially

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[141] The economic effects of easy-to-read disclosure documents are quantified in research that demonstrates a decrease in company valuation caused by a decrease in readability of disclosure documents. *See* Byoung-Hyoun Hwang and Hugh Hokwang Kim, *It Pays to Write Well*, 124 Journal of Financial Economics 373 (2017).

[142] Using the Plain Writing Act as an exogenous event, research has found that the Plain Writing Act resulted in improved readability of Form 10-Ks that caused the risk of stock price crash to fall. *See* Shiyan Yin, Thanaset Chevapatrakul, and Kai Yao, *The Causal Effect of Improved Readability of Financial Reporting on Stock Price Crash Risk: Evidence from the Plain Writing Act of 2010*, 216 Economics Letters (2022). Research has also found that while readability of disclosures improved following the Plain English Disclosure rule, improved readability does not appear to influence more experienced market participants, as measured by equity analysts' earnings forecasts. *See* Samuel B. Bonsall IV, Andrew J. Leone, Brian P. Miller, and Kristina Rennekamp, *A Plain English Measure of Financial Reporting Readability*, 63 Journal of Accounting and Economics 329 (2017).

the language of the standards themselves, but also from third parties (e.g., media) who may write about PCAOB standards. Standards that are not modernized could contribute to an expectation gap—in this case, a gap between what investors expect from an audit and what auditing standards require.[143] Such a gap could in principle exist in either direction. Investors could be led to expect more than what an audit is required to deliver, and thereby fail to price the risk appropriately. Alternatively, investors could be led to expect less than what an audit is required to deliver, and thereby fail to appreciate the important functions performed by auditors regarding reasonable assurance.

Audit committees may also form inaccurate expectations about the content of PCAOB standards if the standards are not modernized, via mechanisms similar to investors. Given audit committee members' greater familiarity with auditing through their position and responsibilities with the issuer and other relevant professional background, we believe this is less likely to occur for audit committees than for investors. However, the negative impact of an audit committee member failing to correctly comprehend the auditor's general responsibilities under PCAOB standards could be more severe, given the audit committee's role in supervising the audit and the auditor under Sarbanes-Oxley for the benefit of investors.

We did not receive comments that provided additional information regarding useability of modernized auditing standards.

#### ii. Clarification of engagement partner responsibilities

One of the responsibilities of engagement partners is to review the work of engagement team members. Any uncertainty under the standards may give engagement partners an incentive, particularly under time pressures, to de-emphasize or omit the review of workpapers. For example, the Board has found instances in which engagement partners did not fulfill their responsibilities for review.[144] However, engagement partner review of workpapers is a critical step to promote audit quality. As noted in Section IV.A.2, firms have varying policies and tools to facilitate the review required by the engagement partner.

One commenter, an academic, referenced academic studies regarding engagement partner impacts. The commenter reported that one study using data from Taiwan finds

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[143] Research finds evidence of a persistent gap between investors' expectations of an audit and auditors' performance based on requirements under auditing standards. *See, e.g.*, Klaus Ruhnke and Martin Schmidt, *The Audit Expectation Gap: Existence, Causes, and the Impact of Changes*, 44 Accounting and Business Research 572, 592 (2014) (finding that the public has expectations of auditors' responsibilities that do not exist under auditing standards, such as conducting a management audit) and ACCA Report (finding that the persistence of the audit expectation gap reflects, in part, the fact that public expectations of audits can grow in line with what auditors can accomplish).

[144] *See, e.g.*, *In the Matter of Jin Tae Kim*, PCAOB Rel. No. 105-2022-013 (Aug. 16, 2022) and *In the Matter of KPMG Assurance and Consulting Services LLP and Sagar Pravin Lakhani*, PCAOB Rel. No. 105-2022-033 (Dec. 6, 2022).

evidence that suggests there is variation in the quality of engagement partners and that the market responds to engagement partner quality.[145] In addition, the commenter reported that a group of studies finds evidence that engagement partners can negatively impact audit quality when they do not follow auditing standards, such as by not promoting the need for professional skepticism, ethical behavior, and continuing education.[146] The views shared by the commenter align with our identification of the need to clarify the engagement partner's responsibility to review certain audit documentation.

### iii. Accelerating the documentation completion date

Section III.B.6 and Section III.C.3 emphasize the importance of adequate audit documentation and the auditor's responsibilities for documentation under AS 1215, which currently specifies an audit documentation completion date no more than 45 days after the report release date. PCAOB standards require auditors to complete all necessary auditing procedures, review those procedures, and obtain sufficient appropriate audit evidence prior to the report release date. The extant requirements were established in part because documentation that is added well after the completion of an audit is likely to be of lesser quality than documentation produced contemporaneously when audit procedures are performed because reconstructing and recalling activities related to performing audit procedures long after the work was actually performed can be difficult.[147] Separately, significant advancements in electronic audit tools and the use of audit software have occurred over the last two decades, which facilitate contemporaneous documentation and more timely documentation completion. Based on these observations and some firms' policies and practices summarized in Section IV.A.3, the current documentation completion date that is 45 days after the report release date may provide more time than necessary to complete and finalize the audit documentation.

The PCAOB inspection process generally cannot begin until after the documentation completion date. In cases where the PCAOB would like to initiate inspections earlier, the 45-day period imposes an unnecessarily long lag before the PCAOB can provide notice of inspection and obtain access to audit documentation, which may prevent timely identification and

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145 *See, e.g.*, Daniel Aobdia, Chan-Jane Lin, and Reining Petacchi, *Capital Market Consequences of Audit Partner Quality*, 90 The Accounting Review 2143 (2015).

146 *See, e.g.*, Sean A. Dennis and Karla M. Johnstone, *A Field Survey of Contemporary Brainstorming Practices*, 30 Accounting Horizons 449 (2016); Harding and Trotman, *The Effect of Partner* 111; Christopher Koch and Steven E. Salterio, *The Effects of Auditor Affinity for Client and Perceived Client Pressure on Auditor Proposed Adjustments*, 92 The Accounting Review 117 (2017); and William F. Messier, Jr. and Martin Schmidt, *Offsetting Misstatements: The Effect of Misstatement Distribution, Quantitative Materiality, and Client Pressure on Auditors' Judgments*, 93 The Accounting Review 335 (2018).

147 *See* PCAOB Rel. No. 2004-006.

resolution of audit deficiencies and delay information on firm performance that is useful to investors for assessing attributes such as audit quality or auditor effort.[148]

As discussed in the proposal, the 45-day period also may pose a greater risk of improper alteration of audit documentation because it provides a lengthy window of opportunity between the release of the audit report and the completion of the audit documentation.[149]

We did not receive comments that provided additional information regarding the need to accelerate the documentation completion date.

### 2. How the Changes Address the Need

#### i. Modernization of the foundational standards

The changes modernize the foundational standards by reorganizing and consolidating four standards, eliminating language that is no longer relevant, establishing conformity with the structure of Board-issued standards, and harmonizing with PCAOB standards and rules issued after the adoption of interim standards in 2003. These changes are designed to make AS 1000 a more effective and efficiently used standard through a well-organized presentation with relevant language that is more consistent with other PCAOB standards.

#### ii. Clarification of engagement partner responsibilities

The changes clarify engagement partner responsibilities by specifying the engagement partner's due professional care responsibilities, explicitly stating that the engagement partner has primary responsibility for the engagement that is not reduced when assistance is provided by other engagement team members, and explicitly stating that audit documentation must clearly demonstrate the person or persons who reviewed the work and the date of such review. Clarification of the engagement partner's responsibility to review certain audit documentation—including review of documentation of significant findings or issues and review of documentation that is required to be reviewed by the EQR—reaffirms the existing minimum

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[148] *See, e.g.*, Jagan Krishnan, Jayanthi Krishnan, and Hakjoon Song, *PCAOB International Inspections and Audit Quality*, 92 The Accounting Review 143 (2017) (finding evidence consistent with improvements in audit quality for foreign firms after PCAOB inspections) and Daniel Aobdia, *The Impact of the PCAOB Individual Engagement Inspection Process—Preliminary Evidence*, 93 The Accounting Review 53 (2018) (finding increases in auditor effort subsequent to deficiencies found through PCAOB inspections). We note that the results from these studies do not necessarily mean that PCAOB inspections cause higher audit quality.

[149] For examples of improper alteration of audit documentation within the 45-day archiving period, *see, e.g.*, *In the Matter of Deloitte LLP*, PCAOB Rel. No. 105-2021-014 (Sept. 29, 2021) and *In the Matter of Richard J. Bertuglia, CPA*, SEC Rel. No. 84419 (Oct. 12, 2018).

level of responsibilities under due professional care and promotes consistency across audits regarding an engagement partner's oversight of the audit.

#### iii. Accelerating the documentation completion date

The changes accelerate the documentation completion date by reducing the maximum period for the auditor to assemble a complete and final set of audit documentation from 45 days to 14 days after the report release date. This change enables PCAOB inspections staff earlier access to audit documentation and reduces the window of opportunity for improper alteration of audit documentation prior to the documentation completion date.

## C. Economic Impacts

This section discusses the expected benefits and costs of the changes and potential unintended consequences. The proposal described expected benefits and costs, resulting in comments on each.[150] Two commenters on the proposal noted that the changes will not result in any significant additional costs to auditors or the companies they audit or in any significant benefits to market participants. Some commenters suggested that the economic analysis should more carefully consider potential costs or unintended consequences associated with certain key provisions, as discussed further below. We expect the economic impacts of AS 1000, including both benefits and costs, to be relatively modest, especially for those firms that have already incorporated in practice an engagement partner's responsibility for review and an accelerated documentation completion date.

### 1. Benefits

#### i. Modernization of the foundational standards

To the extent that current features of the existing foundational standards reduce efficient use of the standards, the changes will help enhance useability by making the general principles and responsibilities of the auditor in conducting an audit in accordance with the standards of the PCAOB easier to read, understand, and apply in practice.

For users trying to navigate and understand the general principles and responsibilities, efficiency gains may be associated with each of the changes as follows:

- The change to reorganize and consolidate the standards into a single standard will reduce time and attention required to navigate several standards to locate the general principles and ensure relevant requirements are met.

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150 *See* PCAOB Rel. No. 2023-001, at 45-50.

- The changes to eliminate language that is no longer relevant will reduce time and attention required to read, understand, and apply the standard by facilitating a focus on core requirements of the standard.

- The changes to establish conformity with the structure of Board-issued standards and make certain enhancements will help expedite navigation of the requirements and ensure relevant requirements are met by: (i) providing more uniformity among the PCAOB standards with an introduction and objectives that emphasize the auditor's obligations; (ii) updating the articulations of the concepts of due professional care, professional skepticism, professional judgment, and reasonable assurance; (iii) clarifying auditor responsibilities by expressing the requirements using Rule 3101 terms; and (iv) minimizing explanatory material that is instead included in the release discussion.

- The changes to harmonize with PCAOB standards and rules issued after adoption of the interim standards in 2003 will reduce time and attention required to read, understand, and apply the standard by drawing attention to: (i) changes to auditing requirements through Board-issued standards; (ii) clarifying the meaning of present fairly; (iii) an overarching objective for audits of ICFR; and (iv) new rules issued by the Board.

Auditors learning the general principles and responsibilities for the first time may do so more quickly and easily, thereby reducing the cost of training and potentially facilitating the newer auditor's ability to perform PCAOB audits.

While the obligation of auditors would not change, reaffirming the auditor's obligation to protect investors could serve as a reminder. Especially to the extent that auditors do not currently fulfill this obligation, it may prompt auditors to reflect on a sense of obligation to investors and the public that goes beyond their responsibilities to a specific company under audit. At the margins, the emphasis on investor protection could reinforce support for auditors in circumstances where they face decisions that may require them to prioritize the interests of the public over their own interests or the interests of the company under audit. Further, by highlighting the important role auditors play in protecting investors, it could underscore the value of the auditing profession to capital markets.

In addition, a modernized standard may enhance investors' and audit committees' awareness and understanding of the auditor's responsibilities. Investors could be able to more appropriately assess financial statement risk by better understanding the nature and extent of auditor responsibilities. Audit committees' oversight of the auditor could be enhanced, for example, if enhanced clarity of standards facilitates communication between the audit committee and the auditor. Referencing academic research, one commenter on the proposal explained that the role of the audit committee in ensuring the quality of reported financial

results requires improved and expanded dialogue between the audit committee and the auditor.[151]

### ii. Clarification of engagement partner responsibilities

To the extent that engagement partners currently do not fulfill their responsibilities for an appropriate review of the work of other engagement team members as required under the existing standards,[152] the clarification of engagement partner responsibilities could improve auditor performance and audit quality by: (i) improving the timeliness of the engagement partner's evaluation of significant findings and judgments; (ii) enhancing the ability of the engagement partner to prevent or detect audit deficiencies; and (iii) facilitating improvements in the quality of the work of other engagement team members. As summarized in Section IV.B.1, one commenter referenced academic studies that suggest engagement partners can negatively impact audit quality when they do not follow auditing standards.

### iii. Accelerating the documentation completion date

The amendment to accelerate the documentation completion date by reducing the maximum period for the auditor to assemble a complete and final set of audit documentation from 45 days to 14 days after the report release date will promote contemporaneous documentation and more timely documentation completion. Documentation that is produced contemporaneously when audit procedures are performed and then completed soon thereafter is likely to provide a more accurate and complete audit file for the engagement. The amendment will also support PCAOB efforts to enhance audit quality via timelier identification and potential resolution of audit deficiencies in cases where inspections are initiated earlier. In such cases, the amendment could facilitate earlier issuance of inspection reports and their availability to investors. In addition, the amendment could enhance auditor performance and audit quality for firms that do not currently implement best practices, but will be more inclined to do so, by proactively focusing on sequencing of work, allocation of resources, and other operating practices.

The benefits associated with an accelerated documentation completion date are likely to be greater for firms that currently make use of the entire 45-day period permitted under current PCAOB standards due to current operating circumstances. These firms would need to make more adjustments to their sequencing of work and allocation of effort to meet the accelerated period. Thus, the concomitant benefits to audit quality would therefore be greater. Based on firms' current archiving policies and practices summarized in Section IV.A.3, the

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[151] *See, e.g.*, Jeffrey Cohen, Lisa Milici Gaynor, Ganesh Krishnamoorthy, and Arnold M. Wright, *Auditor Communications with the Audit Committee and the Board of Directors: Policy Recommendations and Opportunities for Future Research*, 21 Accounting Horizons 165 (2007).

[152] *See, e.g.*, *Jin Tae Kim*, PCAOB Rel. No. 105-2022-013 and *KPMG Assurance and Consulting Services LLP*, PCAOB Rel. No. 105-2022-033.

benefits associated with an accelerated documentation completion date are likely to be higher for NAFs than for GNFs in cases where NAFs experience operating efficiencies associated with changes in their sequencing of work, allocation of resources, and other operating practices to comply with the documentation completion date.

The benefits associated with an accelerated documentation completion date will be lower for firms that already either: (i) have a policy that requires that documentation be completed in 14 days or fewer or (ii) have a policy that is closer to or equal to the current 45-day period but in practice complete their documentation shortly after releasing the audit report. Specifically, the benefits to audit quality will be lower for these firms, but the benefits to investors of earlier PCAOB inspections will still be achieved in cases where inspections are initiated earlier.

Commenters on the proposal generally agreed that accelerating the documentation completion date is feasible for firms and beneficial to investors. One commenter suggested the ability to inspect audits sooner is a benefit that will not significantly increase costs. Another commenter, an academic, suggested there could be market benefits associated with earlier inspections if inspection reports are publicly available earlier and the content of inspection reports is meaningful. The commenter referenced several academic studies that demonstrate improvements in audit quality after PCAOB inspections.[153] The commenter reported that one study finds improvements in internal control audits after PCAOB inspections[154] and that another study finds increases in auditor effort after PCAOB inspections find audit deficiencies.[155] One commenter questioned whether accelerating the documentation completion date would have any meaningful impact on inspection timelines. Based on the acceleration of the documentation completion date by 31 days, we note that the most an inspection report could be accelerated as a result of the accelerated documentation completion date is 31 days.

### 2. Costs

#### i. Modernization of the foundational standards

The primary costs of the modernization efforts reflected in the standard will be one-time costs to firms for updating references within firm methodologies and related guidance to reflect the final standard and related amendments. Larger firms that develop their own methodologies will update references directly in those methodologies. Smaller firms generally purchase methodologies from third-party vendors. The implementation costs of the changes

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153 *See, e.g.*, Krishnan, et al., *PCAOB International Inspections*. We note that the results from these studies do not necessarily mean that PCAOB inspections cause higher audit quality.

154 *See, e.g.*, Mark L. DeFond and Clive S. Lennox, *Do PCAOB Inspections Improve the Quality of Internal Control Audits?* 55 Journal of Accounting Research 591 (2017).

155 *See, e.g.*, Aobdia, *The Impact of the PCAOB*.

may be offset over time because a more logical and easy-to-read-and-navigate standard could enable auditors to save time reading, understanding, and applying the standard. Third parties that refer to PCAOB standards (e.g., in textbooks, training, or review materials) will also need to update those materials.

To the extent that auditors are not taking into account PCAOB auditing interpretations, as used in paragraph .15 and the related note of the standard, those firms will also incur one-time and ongoing costs related to methodology and periodic training for PCAOB auditing interpretations.

To the extent that auditors do not currently fulfill their obligation to protect investors, auditors who face decisions that require them to prioritize the interests of the public over their own interests or the interests of the company under audit may make decisions that benefit the public at a potential cost to the auditor, such as alienating or losing a company under audit. There is likely already a balance struck between fulfilling the auditor's obligation to protect investors and the risk of alienating or losing a company under audit. At the margins, the emphasis on investor protection may move the fulcrum closer to the public interest.

We did not receive comments that provided additional information regarding costs of modernization.

**ii. Clarification of engagement partner responsibilities**

To the extent that engagement partners currently do not fulfill their responsibilities for an appropriate review of the work of other engagement team members as required under the existing standards,[156] those firms may incur one-time costs to update firm methodologies and ongoing costs related to fulfilling their responsibilities. Larger firms that develop their own methodologies will update references directly in those methodologies. Smaller firms generally purchase methodologies from third-party vendors.

While the responsibilities of engagement partners would not change under the new standard, the clarification for engagement partners to perform their duties with due professional care, including their responsibility for performing an appropriate review of the work of other engagement team members, could also impose incremental costs related to fulfilling engagement partner responsibilities to the extent that engagement partners are not currently fulfilling their responsibilities.

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[156] *See, e.g.*, *Jin Tae Kim*, PCAOB Rel. No. 105-2022-013 and *KPMG Assurance and Consulting Services LLP*, PCAOB Rel. No. 105-2022-033.

One commenter reported that research highlights the importance of and variation in the direction, supervision, and review of audit work.[157] The commenter further noted that direction, supervision, and review are functions that are performed by auditors at different levels of experience, not just engagement partners, and cited research that highlights that the effectiveness of the functions can vary across hierarchical levels.[158] While we acknowledge the commenter's points regarding the effectiveness of functions performed by auditors at different levels of experience, our analysis of costs here is limited to costs that are relevant to the economic impacts of the clarification of engagement partner responsibilities.

### iii. Accelerating the documentation completion date

The amendment to accelerate the documentation completion date by reducing the maximum period for the auditor to assemble a complete and final set of audit documentation from 45 days to 14 days after the report release date will allow less time to assemble the final set of workpapers after the audit report is released. However, the PCAOB requirement to complete necessary auditing procedures, review those procedures, and collect sufficient appropriate audit evidence prior to the report release date could help mitigate costs to implement the amendment because the only activities that remain are assembling a complete and final set of audit documentation. In addition, the widespread use of electronic audit tools and audit software could help mitigate any costs associated with the amendment.

The costs associated with an accelerated documentation completion date are likely to be greater for firms that currently specify by policy an archiving period that is near or equal to the maximum permitted under current AS 1215.15 and that currently take all or nearly all of the full 45-day period to complete their archiving because of operating circumstances that inhibit faster completion. These firms will have to invest additional resources to enhance sequencing of their work, allocation of resources, and other operating practices, or may have to enhance their audit documentation systems, or both, in order to comply with the documentation completion date. Based on firms' current archiving policies and practices summarized in Section IV.A.3, the costs associated with an accelerated documentation completion date are likely to be higher for NAFs than for GNFs in cases where NAFs currently use the entire 45-day period. However, the extended effective date of the 14-day requirement for firms that issued audit reports with respect to 100 or fewer issuers during the calendar year ending December 31, 2024, will allow those firms more time to implement the revised

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[157] *See, e.g.*, J.S. Rich, I. Solomon, and K.T. Trotman, *The Audit Review Process: A Characterization from the Persuasion Perspective*, 22 Accounting, Organizations & Society 481 (1997) and Mark Nelson and Hun-Tong Tan, *Judgment and Decision Making Research in Auditing: A Task, Person, and Interpersonal Interaction Perspective*, 24 Auditing: A Journal of Practice & Theory 41 (2005).

[158] *See, e.g.*, Robert J. Ramsay, *Senior/Manager Differences in Audit Workpaper Review Performance*, 32 Journal of Accounting Research 127 (1994) and Noel Harding and Ken T. Trotman, *Hierarchical Differences in Audit Workpaper Review Performance*, 16 Contemporary Accounting Research 671 (1999).

requirement. By contrast, GNFs that already require the completion of documentation within a 14-day period will likely not incur substantial additional costs to comply with the revised requirement.

Electronic audit tools and audit software may facilitate compliance with the requirement by automating, and thereby performing more quickly, certain processes. For firms without electronic systems in place, costs associated with an accelerated documentation completion date may include additional resources, such as in-house personnel or capital investments in audit software, to help assemble a complete and final set of audit documentation in the 14-day time period. PCAOB staff is aware that some small NAFs still use paper-based systems. However, these firms generally perform smaller, less complex audits, such that the firms do not have to mail audit workpapers from multiple locations; therefore, even with a paper-based system, effective sequencing of work, allocation of resources, and other operating practices could enable them to meet the 14-day documentation completion date.

For firms with electronic audit tools and audit software in place, the earlier documentation completion date should not change the functionality or cost of software, which will facilitate a low-cost transition to the new archiving period. Some firms already have policies that require documentation completion within 14 days of the report release date, and some firms require audit documentation to be archive-ready upon completion of interim procedures. These practices suggest that much of the process involved in assembling a complete and final set of audit documentation, such as assembly, cleanup, and retention, is substantially finished in advance of 45 days. Any firms that currently have a policy or practice of completing audit documentation on or near the 45$^{th}$ day may do so merely because the current standard allows 45 days, and thus will not incur costs to meet the accelerated documentation completion date. Alternatively, any firms that currently complete audit documentation on or near the 45$^{th}$ day because of operating circumstances may incur costs associated with implementing best practices to effectively sequence work, allocate resources, and incorporate other operating practices to comply with the accelerated documentation completion date. In this case, we anticipate that the costs will be offset over time by improvements in operating efficiencies to the extent that operating circumstances are within the firm's control.

An accelerated documentation completion date may also impose costs on multi-firm audits if electronic audit documentation systems are not integrated across firms. GNFs are more likely than NAFs to perform multi-firm audits, but some NAFs do perform multi-firm audits.[159] If electronic systems are not integrated across firms, which is more likely for NAFs, other auditors may need to transmit documentation to the lead auditor to assemble the final set of workpapers. If electronic systems are integrated across firms, the lead auditor may be able to seamlessly archive the work of other auditors.

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[159] *See* PCAOB Rel. No. 2022-002, at 26-52.

Any costs associated with the requirements may be passed through to investors, or costs may be internalized by firms. While competition in the audit market is characterized by a combination of unique features,[160] issuers that engage firms that pass through any costs may switch firms if the benefits of switching justify the costs of switching.

Some commenters noted potential costs associated with accelerating the documentation completion date. One commenter generally supported accelerating the documentation completion date but noted that firms that use proprietary audit tools and audit software will incur costs related to reprogramming and testing that could be exacerbated for GNFs that are subject to differing jurisdictional requirements. The same commenter also noted that accelerating the documentation completion date may negatively impact smaller firms that do not utilize electronic audit tools to the extent that they are unable to comply with the requirement without considerable investments that may not be economically feasible. Another commenter disagreed with accelerating the date because of human capital factors and a complex auditing landscape. Another commenter reported that academic research investigating the SEC's acceleration of Form 10-K filing deadlines in the 2000s suggests that accelerating the filing deadlines more quickly than 15 days was costly to issuers regarding misstated financial statements.[161] The commenter acknowledged the analogy may not align with the documentation completion date but suggested that it is likely that firms currently requiring more than 29 days to complete audit documentation will likely incur non-trivial compliance costs.

We acknowledge that firms that use proprietary audit tools and audit software will incur costs related to reprogramming and testing. While we also acknowledge that some smaller firms may incur costs related to investments and some firms may incur costs related to human capital or a complex auditing landscape, we believe that most firms will incur incremental costs because they already use electronic audit documentation systems. Likewise, we believe the contrast between the SEC's acceleration of Form 10-K reporting deadlines and our acceleration of the documentation completion date is too stark to be a useful comparison because the auditing standards require that all necessary auditing procedures, review of those procedures, and collection of sufficient appropriate audit evidence be completed prior to the report release date. Based on the broad support by commenters for accelerating the documentation

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[160] *See, e.g.*, Joseph Gerakos and Chad Syverson, *Competition in the Audit Market: Policy Implications*, 53 Journal of Accounting Research 725 (2015) (explaining that the audit market exhibits a set of features that distinguish it from other markets for business services, including its role in capital market transparency, mandated demand, and concentrated supply).

[161] *See, e.g.*, Lisa Bryant-Kutcher, Emma Yan Peng, and David P. Weber, *Regulating the Timing of Disclosure: Insights from the Acceleration of 10-K Filing Deadlines*, 32 Journal of Accounting and Public Policy 475 (2013); Colleen M. Boland, Scott N. Bronson, and Chris E. Hogan, *Accelerated Filing Deadlines, Internal Controls, and Financial Statement Quality: The Case of Originating Misstatements*, 29 Accounting Horizons 551 (2015); and Khaled Alsabah, *The 15-Day Debate and the Value of Early Release of Information: Evidence from 10-K Filings*, 42 Journal of Accounting and Public Policy 1 (2023).

completion date and the existing requirement that all necessary auditing procedures, review of those procedures, and collection of sufficient appropriate audit evidence be completed prior to the report release date, we continue to believe that accelerating the documentation completion date by reducing the maximum period for the auditor to assemble a complete and final set of audit documentation from 45 days to 14 days after the report release date will provide better protection for investors.

One commenter suggested that keeping the 35-day filing requirement for Form AP in light of accelerating the documentation completion date could create technological and process challenges for firms. Another commenter suggested that firms could incur incremental costs such as process changes and administrative costs. In contrast, some commenters said they would not have difficulty filing Form AP within 35 days of the audit report being filed with the SEC. Two commenters suggested the time to file Form AP should be consistent with the documentation completion date. We are adopting the 14-day deadline for archiving audit documentation. We note that firms, under AS 1215, can add information to the audit documentation after the documentation completion date, if necessary, to record their compliance with Form AP requirements. Consequently, we do not perceive any conflict or a necessity to modify either the 35-day Form AP filing requirement or the proposed 14-day deadline for archiving audit documentation.

### 3. Potential Unintended Consequences

In addition to the benefits and costs discussed above, the final standard and related amendments could have unintended economic consequences. The proposal described potential unintended consequences, which commenters addressed in their letters.[162] This section discusses the potential unintended consequences we have considered as well as our consideration of such consequences in adopting the final standard and related amendments. The discussion also addresses, where applicable, any mitigating or countervailing factors, including revisions to the proposed standard and related amendments reflected in the final standard and related amendments we are adopting.

#### i. Modernization of the foundational standards

The changes to modernize the foundational standards are not intended to impose new requirements on auditors or substantially change the requirements of PCAOB standards.

Commenters noted potential unintended consequences related to the removal of explanatory language or the use of certain language in the proposed rule text or release discussion. Several commenters suggested that removing explanatory language on limitations of an audit may exacerbate the audit expectation gap and cause potential confusion among auditors. Commenters also suggested that the use of certain proposed language or certain proposed clarifications could result in potential confusion or unintended expansion of auditors'

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[162] *See* PCAOB Rel. No. 2023-001, at 50-51.

responsibilities. For example, one commenter suggested that requiring auditors to "keep in mind their role in protecting investors" could encourage auditors to adopt an investor perspective when making judgments, which research highlights may be detrimental to audit quality.[163]

These potential unintended consequences will be mitigated by changes to language in the adopted rule text or release discussion. Throughout the rulemaking process, we have emphasized that eliminating restrictive provisions does not alter the core principles and responsibilities that are transitioned from the current standards to AS 1000. We removed the reference to "keep in mind their role in protecting investors" from the final standard based on changes made to paragraph .01 of the final standard. While we have emphasized the investor protection obligation, we have clarified that the emphasis does not create any new legal requirements. We do not believe that highlighting the auditor's existing obligation to protect investors will widen any expectation gap or decrease audit quality. Instead, our goal is to heighten auditors' awareness and reinforce their existing obligation.

### ii. Clarification of engagement partner responsibilities

An unintended consequence of the amendment to clarify engagement partner responsibilities would occur if, contrary to the Board's expectation, some firms whose engagement partners currently do more than will be required to meet the minimum requirement for engagement partner review, do less in the future to merely meet the minimum requirement.[164]

This potential unintended consequence will be mitigated by the extent to which engagement partners are aware that the engagement's performance is primarily their responsibility. Furthermore, in contrast to a highly specific minimum threshold, we note that engagement partners under AS 1000 are bound to broad due professional care responsibilities that are less likely to incentivize engagement partners to merely meet a precise set of criteria without exceeding those criteria. In addition, economic reasons that generate enhanced performance in the first place, such as partner compensation, inspections, and litigation threat, help to mitigate this potential unintended consequence.

One commenter suggested that the amendment to clarify engagement partner responsibilities is reasonable and clear but could present unintended consequences by limiting

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[163] *See, e.g.*, Elizabeth C. Altiero, Yoon Ju Kang, and Mark E. Peecher, *Motivated Perspective Taking: Why Prompting Auditors to Take an Investor's Perspective Makes Them Treat Identified Audit Differences as Less Material*, 39 Contemporary Accounting Research 339 (2022) and Lei Dong, Lei Wang, and Wen-Wen Chien, *The Joint Effect of Supervisor Influence and Investor Perspective: Unintended Consequences on Assessing Accounting Estimates*, 37 Managerial Auditing Journal 151 (2022).

[164] *See, e.g.*, Aobdia, *The Impact of the PCAOB* (finding that auditor effort declines subsequent to PCAOB inspections of engagements that do not receive a Part I finding).

firms' abilities to attract and retain talent, which could potentially result in lower audit quality if people leave the profession. We anticipate that the amendments related to engagement partner responsibilities will be unlikely to significantly affect firms' abilities to attract or retain talent, or to disincentivize individuals from being willing to serve as engagement partners because AS 1000 clarifies existing engagement partner responsibilities. As outlined in the rest of the economic analysis, we acknowledge that some marginal economic impacts could follow from these amendments, but we do not agree with the commenter that those effects will be dramatic.

#### iii. Accelerating the documentation completion date

Unintended consequences of accelerating the documentation completion date would occur if, contrary to the Board's expectation, (i) auditor time prior to the report release date that was previously spent focusing on audit procedures is now spent on assembling final workpapers or (ii) the archiving period results in higher costs that cause firms with paper-based documentation systems to exit the audit market or to not enter the audit market.

These potential unintended consequences will be mitigated by the current requirement that all necessary auditing procedures, review of those procedures, and collection of sufficient appropriate audit evidence be completed prior to the report release date.[165] Furthermore, if firms proactively sequence work, allocate resources, and incorporate other operating efficiencies, they should not experience substantial disruptions and should be able to handle the accelerated archiving deadline without major problems.

One commenter acknowledged that accelerating the documentation completion date may enhance audit quality overall but suggested that it could have an initial negative impact on audit quality as a result of accelerating the archiving process into the period when many SEC practice audit professionals need to start working on other issuer audit engagements. Another commenter also acknowledged that accelerating the documentation completion date may enhance audit quality and said it may allow PCAOB inspections to begin sooner after completion of an audit, but issuers may have various filing deadlines or require extensions that will necessitate the full attention of professionals on those engagements. One commenter acknowledged that the acceleration is beneficial and appropriate, but suggested that beginning the inspection process earlier could be detrimental to audit quality because earlier inspections could cause auditors to reallocate their time to the inspection process and away from audits of financial statements. Consistent with the acknowledgements by these commenters, we continue to believe that accelerating the documentation completion date will be facilitated by the widespread use of electronic audit tools and audit software by most firms, which could mitigate potential operating disruptions that firms experience as they adjust to the accelerated date.

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165 *See* AS 1215.15.

One commenter stressed the importance of the quality of audit documentation and noted that technology interruptions or cybersecurity matters could impact the ability of a firm to meet the accelerated deadline. However, the possibility of technology interruptions or cybersecurity matters could impact a firm's ability to meet any deadline. Another commenter reported that academic studies find there can be unintended consequences of additional regulation, including new costs associated with extensive audit documentation, auditors taking a "box-ticking" approach to extensive documentation requirements, and reduced auditor retention.[166] However, accelerating the documentation completion date does not add any new documentation requirements.

## D. Alternatives Considered

During the formulation of the proposal and adoption of the final standard and related amendments, we considered a number of alternative approaches to the final standard and related amendments we are adopting, including those suggested by commenters.

### 1. Modernization of the Foundational Standards

We considered whether to update the foundational standards and keep them as individual standards, but we believe that combining the general principles and responsibilities into one standard is more logical and easier to navigate. This approach is also consistent with the approaches of other standard setters. For example, both the IAASB and the ASB address general responsibilities of the auditor in one standard (see IAASB's ISA 200 and ASB's AU-C 200).

We have also considered whether to incorporate the requirements of AS 2815 into AS 1000, but we believe that it is more logical to incorporate the requirements of AS 2815 into AS 2810 because both standards address requirements for concluding audit procedures. This approach also eliminates unnecessary cross-references between the two standards and makes the auditor's responsibilities easier to locate. AS 1000 includes a reference to AS 2810 for the auditor's responsibilities related to the evaluation of whether the financial statements are presented fairly, in all material respects, in conformity with the applicable financial reporting framework.

### 2. Clarification of Engagement Partner Responsibilities

With respect to engagement partner responsibilities, we considered retaining the language of AS 1010 that describes the use of judgment in the context of the partner's

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[166] *See, e.g.*, Colleen M. Boland, Brian E. Daugherty, and Denise Dickins, *Evidence of the Relationship between PCAOB Inspection Outcomes and the Use of Structured Audit Technologies*, 38 Auditing: A Journal of Practice & Theory 57 (2019) and Marion Brivot, Mélanie Roussy, and Maryse Mayer, *Conventions of Audit Quality: The Perspective of Public and Private Company Audit Partners*, 37 Auditing: A Journal of Practice & Theory 51 (2018).

responsibilities for supervision. However, we believe that leveraging the requirements of AS 1201, a more recent standard, avoids potential confusion and aligns the engagement partner's responsibilities with Board-issued standards. Other alternatives to the amendments related to engagement partner responsibilities, including comments received, were considered as discussed in Section III.B.4 and Section III.C.2.

### 3. Accelerating the Documentation Completion Date

For the documentation completion date, we considered a length of time between the current 45-day period and the 14-day period, such as 21 days or 30 days. We believe that a shorter period of time may provide better protection for investors than a longer period: it could permit acceleration of PCAOB inspections and provide the strongest incentives for firms to implement operating efficiencies that may ultimately improve audit quality. Thus, in principle, a shorter documentation completion date could achieve more benefits than a longer period. Our assessment of existing firm practice as described in Section IV.A.3 leads us to believe that 14 days is feasible for firms and that a longer period could therefore be unnecessary and would erode the benefits that would otherwise be achieved.

Investor-related groups suggested the documentation completion date should be reduced to two days for all firms. We continue to believe 14 days is feasible for all firms while not being too restrictive for firms that may require more time. Another commenter asserted that the economic analysis did not adequately consider alternatives other than 14 days and that the analysis did not offer any alternatives to begin inspections earlier other than accelerating the documentation completion date. As noted above, we considered a length of time between the current 45-day period and the 14-day period. Moreover, the need to accelerate the documentation completion date is based on other considerations in addition to cases where the PCAOB would like to initiate inspections earlier. Another commenter asserted that firms' operating efficiencies are not the purview of the PCAOB. However, the need for the amendment is not based on operating efficiencies but may result in operating efficiencies that improve audit quality.

We also considered whether to specify different documentation completion dates for different classes of firms, based on specific firm characteristics that may make compliance with an accelerated documentation completion date especially challenging because of some practical obstacle or because of expenses that are common to that class of firms. For example, we considered specifying a longer documentation completion date for NAFs than for GNFs. However, as noted above, we believe that the 14-day period is a feasible period for all firms; we are not aware of any practical obstacle or expenses that will make compliance with a 14-day period especially challenging for all firms within a particular class. In contrast, a uniform and consistent archiving period for all firms would facilitate implementation and compliance, especially for audits that involve multiple firms that could be subject to different archiving

periods. Finally, having a unified archiving date will enable earlier PCAOB inspections across all registered firms.[167]

## V. SPECIAL CONSIDERATIONS FOR AUDITS OF EMERGING GROWTH COMPANIES

Pursuant to Section 104 of the Jumpstart Our Business Startups ("JOBS") Act, rules adopted by the Board subsequent to April 5, 2012, generally do not apply to the audits of emerging growth companies ("EGCs"), as defined in Section 3(a)(80) of the Exchange Act, unless the SEC "determines that the application of such additional requirements is necessary or appropriate in the public interest, after considering the protection of investors, and whether the action will promote efficiency, competition, and capital formation."[168] As a result of the JOBS Act, the rules and related amendments to PCAOB standards that the Board adopts are generally subject to a separate determination by the SEC regarding their applicability to audits of EGCs.[169]

To inform consideration of the application of auditing standards to audits of EGCs, PCAOB staff prepares a white paper annually that provides general information about characteristics of EGCs.[170] As of the November 15, 2022 measurement date, there were 3,031 companies[171] that self-identified as EGCs and filed audited financial statements with the SEC

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[167] While we have not specified different documentation completion dates for different classes of firms, the extended effective date of the 14-day requirement for firms that issued audit reports with respect to 100 or fewer issuers during the calendar year ending December 31, 2024, will allow those firms more time to implement the revised requirement.

[168] *See* Pub. L. No. 112-106 (Apr. 5, 2012). Section 103(a)(3)(C) of Sarbanes-Oxley, as added by Section 104 of the JOBS Act, also provides that any rules of the Board requiring (1) mandatory audit firm rotation or (2) a supplement to the auditor's report in which the auditor would be required to provide additional information about the audit and the financial statements of the issuer (auditor discussion and analysis) shall not apply to an audit of an EGC. The new standard does not fall within either of these two categories.

[169] We are providing this analysis of the impact on EGCs to assist the SEC in making the determination required under Section 104 to the extent that the requirements apply to "the audit of any emerging growth company" within the meaning of Section 104 of the JOBS Act.

[170] *See* PCAOB, *Characteristics of Emerging Growth Companies and Their Audit Firms at November 15, 2022* (Feb. 20, 2024) ("EGC White Paper"), *available at* https://assets.pcaobus.org/pcaob-dev/docs/default-source/economicandriskanalysis/projectsother/documents/white-paper-on-characteristics-of-emerging-growth-companies-as-of-nov-15-2022.pdf?sfvrsn=a8294f3_2.

[171] The EGC White Paper uses a lagging 18-month window to identify companies as EGCs. Please refer to the "Current Methodology" section in the EGC White Paper for details. Using an 18-month window enables staff to analyze the characteristics of a fuller population in the EGC White Paper but may tend to result in a larger number of EGCs being included for purposes of the present EGC analysis

between May 16, 2021, and November 15, 2022, that included an audit report signed by a firm.[172]

As discussed in the proposal, the economic impacts of the standard and related amendments are generally applicable to audits of EGCs.[173] The amendment to accelerate the documentation completion date by reducing the maximum period for the auditor to assemble a complete and final set of audit documentation from 45 days to 14 days could impact the audits of EGCs more than the audits of non-EGCs to the extent that EGCs are more likely than non-EGCs to be audited by NAFs.[174] As discussed in Section IV.C, NAFs are expected to require more changes than GNFs in their sequencing of work, allocation of resources, and other operating practices to comply with the accelerated documentation completion date. Therefore, all else equal, both the benefits and costs of the amendments, including the amendment to accelerate the documentation completion date, may be higher for EGC audits than for non-EGC audits.

While both the benefits and costs of the amendment to accelerate the documentation completion date may be higher for EGC audits, the costs may be mitigated based on certain characteristics of EGCs. For example, to the extent that EGCs are smaller than non-EGCs, EGC audits may be less complex, which potentially facilitates expeditious assembly of the final workpapers.[175] In addition, to the extent that EGCs are audited by firms that issued audit reports with respect to 100 or fewer issuers during the calendar year ending December 31, 2024, the extended effective date of the amendment to accelerate the documentation completion date will allow those firms more time to implement the accelerated documentation completion date.[176] Moreover, as EGCs are not large accelerated filers ("LAFs"), the SEC Form 10-K filing deadline for EGCs is either 75 days after the fiscal year end for accelerated filers or 90 days for non-accelerated filers. This provides firms with an additional 15 days for accelerated

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than would alternative methodologies. For example, an estimate using a lagging 12-month window would exclude some EGCs that are delinquent in making periodic filings. An estimate as of the measurement date would exclude EGCs that have terminated their registration or that have exceeded the eligibility or time limits.

172 *See* EGC White Paper 17. Based on staff analysis as of the Nov. 15, 2022 measurement date, 86 percent of the 263 firms that issued audit reports for EGCs performed audits for both EGC and non-EGC issuers while 14 percent performed issuer audits only for EGCs.

173 *See* PCAOB Rel. No. 2023-001, at 52-54.

174 PCAOB staff analysis indicates that, compared to exchange-listed non-EGCs, exchange-listed EGCs are approximately 2.6 times as likely to be audited by an NAF (source: EGC White Paper and Standard & Poor's).

175 *See* EGC White Paper, Figure 9 and Figure 12 (indicating that exchange-listed EGCs have lower market capitalization and revenue than exchange-listed non-EGCs).

176 *See* EGC White Paper 22. Based on staff analysis as of the Nov. 15, 2022 measurement date, U.S. firms audited 2,548 EGCs, of which 817 were audited by firms that issued audit reports for 100 or fewer issuer audit clients.

filers or 30 days for non-accelerated filers, as compared to the time period for LAFs, to assemble the required final workpapers during a period that may be proportionately less busy.

The amendment to accelerate the documentation completion date could improve efficiency and capital formation for EGCs to the extent that the amendment reduces uncertainty about the reliability of an EGC's financial statements via enhanced audit quality. Investors who are uncertain about the reliability of an EGC's financial statements may require a larger risk premium that reduces the efficient allocation of capital or increases the cost of capital. Thus, any reduction of uncertainty via enhanced audit quality, including from firms' implementation of operating efficiencies, could improve the efficiency of capital allocation, lower the cost of capital, and enhance capital formation for those EGCs.

The amendment to accelerate the documentation completion date could also impact competition in an EGC product market if any indirect costs to audited companies disproportionately affect EGCs relative to their competitors. For example, if EGCs are forced to raise prices in order to remain viable but their non-EGC competitors are not forced to raise prices, this may divert market share toward their non-EGC competitors. This could increase competition in markets where EGCs have a dominant market share and decrease competition in markets where EGCs have a less than dominant market share. However, the incentives for firms to pass costs onto EGCs may also be limited by competition for audits.

The proposal sought comments on the applicability of the proposed requirements to audits of EGCs. Several commenters agreed that the requirements of AS 1000 should apply to the audits of EGCs. One commenter suggested that the audits of EGCs should be subject to stricter requirements because non-accelerated filers have a higher incidence of restatements and because small capitalization issuers have a higher proportion of equity owned by individual investors but less coverage by sell-side analysts.[177] However, we continue to believe the same standard and related amendments should apply to audits of EGCs and non-EGCs to avoid the potential for confusion that could accompany differences within firms' policies and procedures with respect to audits of EGCs and non-EGCs.

Accordingly, and for the reasons explained above, the Board will request that the Commission determine that it is necessary or appropriate in the public interest, after considering the protection of investors and whether the action will promote efficiency, competition, and capital formation, to apply the standard and related amendments to audits of EGCs.

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[177] *See, e.g.*, Audit Analytics, *2021 Financial Restatements: A Twenty-One Year Review* (May 2022) and Garnet Roach, *Only Small Caps See Minority of Shares Held by Institutions, Research Shows*, IR Magazine (Jan. 18, 2022).

## VI. EFFECTIVE DATE

In the proposing release, the Board sought comment on the amount of time auditors would need before the proposed standard and related proposed amendments to PCAOB standards would become effective, if adopted by the Board and approved by the SEC. We proposed an effective date of June 30 of the year after approval by the SEC.

A number of commenters, mostly firms, suggested that an effective date be based on a fiscal year end date (e.g., audits of fiscal years ending on or after December 15) rather than the proposed effective date of June 30 in the year after SEC approval. These commenters generally pointed to challenges associated with a mid-year implementation (e.g., need to update firm methodologies for foundational standards and for performance standards amended by this project, provide training). Specific dates suggested by commenters included: (i) audits of periods beginning on or after December 15, 2024 (assuming 2023 SEC approval); (ii) 12 months after SEC approval; (iii) 18 months after SEC approval; and (iv) 24 months after SEC approval.

In addition, a firm and a firm-related group suggested that we consider the effective dates for other standard-setting projects such as QC 1000 when setting the effective date for AS 1000. In response to commenters, and after considering the effective dates for other Board rulemaking projects, we have revised the effective date for the new standard and related amendments.

Subject to approval by the SEC, the new standard and related amendments will take effect for audits of financial statements for fiscal years beginning on or after December 15, 2024, except for the 14-day documentation completion date requirement (AS 1215.15). For that requirement, we are adopting a phased approach to provide smaller firms more time to prepare for implementation. The requirement will take effect as follows:

- For public accounting firms that, during the calendar year ending December 31, 2024, issued audit reports with respect to more than 100 issuers, the 14-day documentation completion requirement will take effect for audits of financial statements for fiscal years beginning on or after December 15, 2024; and

- For all other registered public accounting firms, the 14-day documentation completion requirement will take effect for audits of financial statements for fiscal years beginning on or after December 15, 2025.

We believe that changing the effective date to fiscal years beginning on or after December 15, 2024 responds to commenters who (i) expressed concerns about having a mid-year implementation and (ii) suggested that an effective date be based on a fiscal year-end date. Given the nature of requirements of the new standard and related amendments, as well as the extent of the differences between the new standard and the foundational standards, we believe that the general effective date will provide auditors with reasonable time to implement the new standard and related amendments. Further, extending the effective date for

implementation of the 14-day documentation completion date requirement responds to the need articulated by commenters to provide smaller firms more time to prepare for implementation.

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On the 13th day of May, in the year 2024, the foregoing was, in accordance with the bylaws of the Public Company Accounting Oversight Board,

ADOPTED BY THE BOARD.

/s/ Phoebe W. Brown

Phoebe W. Brown
Secretary

May 13, 2024

# APPENDIX 1 – Auditing Standard

## AS 1000: General Responsibilities of the Auditor in Conducting an Audit

### INTRODUCTION

.01 The auditor has a fundamental obligation to protect investors through the preparation and issuance of informative, accurate, and independent auditor's reports. This responsibility transcends an auditor's relationship with management and the audit committee of the company under audit, providing the foundation for an objective and independent audit. A properly conducted audit and the related auditor's report enhance the confidence of investors and other financial statement users[1] in the company's financial statements and, if applicable, internal control over financial reporting.

Note: The auditor's obligation to protect investors provides important context to the auditor's work when applying the requirements of this and other Public Company Accounting Oversight Board ("PCAOB") standards and rules.

.02 This standard describes the general principles and responsibilities of the auditor in properly conducting an audit in accordance with the standards of the PCAOB. This standard sets out the objectives of the auditor, establishes requirements for the auditor's professional qualifications and the auditor's general responsibilities applicable in all audits, and describes auditing principles relevant to conducting the audit.

### OBJECTIVES OF THE AUDITOR

.03 The objectives of the auditor are to:

a. In an audit of financial statements – (1) obtain reasonable assurance about whether the financial statements are free of material misstatement, whether due to error or fraud; and (2) issue an auditor's report that expresses an opinion about whether the financial statements, taken as a whole, are presented fairly, in all material respects, in conformity with the applicable financial reporting framework;

b. In an audit of internal control over financial reporting – (1) obtain reasonable assurance about whether material weaknesses exist as of the date specified in management's assessment; and (2) issue an auditor's report that expresses an

[1] This standard uses "investors and other financial statement users" to include a company's existing and potential shareholders, bondholders, lenders, other creditors, and others who use the company's financial statements.

opinion on the effectiveness of the company's internal control over financial reporting;

c. Communicate externally in accordance with **applicable professional and legal requirements**;[2] and

d. Satisfy and fulfill the other general principles and responsibilities described in this standard.

## PROFESSIONAL QUALIFICATIONS OF THE AUDITOR

### Independence and Ethics

.04 The auditor must be independent of the company under audit both in fact and in appearance throughout the audit and professional engagement period.[3] The auditor is not independent with respect to the company under audit if the auditor is not, or a reasonable investor with knowledge of all relevant facts and circumstances would conclude that the auditor is not, capable of exercising objective and impartial judgment on all matters encompassed within the engagement.[4]

.05 The auditor must satisfy the independence criteria set out in the rules and standards of the PCAOB, and satisfy all other independence criteria applicable to the engagement, including the independence criteria set out in the rules and regulations of the U.S. Securities and Exchange Commission ("SEC") under the federal securities laws.[5]

.06 The auditor must comply with applicable ethics requirements, including the ethics rules and standards of the PCAOB.[6]

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[2] The term is defined in Appendix A, *Definition*, and is set in **boldface type** the first time it appears.

[3] *See* PCAOB Rule 3501, *Definitions of Terms Employed in Section 3, Part 5 of the Rules*, for the definition of the term "audit and professional engagement period."

[4] *See* Regulation S-X Rule 2-01, 17 C.F.R. § 210.2-01 for the analogous provision on auditor independence. For the purposes of this standard, the phrase "company under audit" has the same meaning as "audit client" under PCAOB Rule 3501(a)(iv).

[5] *See, e.g.*, Regulation S-X Rule 2-01, 17 C.F.R. § 210.2-01, and Section 3, Part 5 of PCAOB rules. To the extent that a provision of one rule is more restrictive than that of another rule, the auditor is required to comply with the more restrictive provision. *See* PCAOB Rule 3500T, *Interim Ethics and Independence Standards*.

[6] *See, e.g.*, Section 3, Part 5 of PCAOB rules; EI 1000, *Integrity and Objectivity*, which requires auditors to maintain integrity and objectivity.

## Competence

.07 The audit must be performed by an auditor who has the competence to conduct an audit in accordance with applicable professional and legal requirements. Competence consists of having the knowledge, skill, and ability that enable the auditor to perform their assigned activities in accordance with applicable professional and legal requirements and the firm's policies and procedures. Competence is measured both qualitatively and quantitatively.

> Note: Competence includes knowledge and proficiency in accounting and auditing standards and SEC rules and regulations relevant to the company being audited and the related industry or industries in which it operates.

.08 The auditor should develop and maintain competence through an appropriate combination of:

a. Academic education;

b. Professional experience in accounting and auditing, with proper supervision;[7] and

c. Training, including accounting, auditing, independence, ethics, and other relevant continuing professional education.

## DUE PROFESSIONAL CARE, INCLUDING PROFESSIONAL SKEPTICISM

.09 The auditor must exercise due professional care in all matters related to the audit.[8] Due professional care concerns what the auditor does and how well the auditor does it. Due professional care means acting with reasonable care and diligence, exercising professional skepticism, acting with integrity, and complying with applicable professional and legal requirements.[9]

.10 For the engagement partner,[10] due professional care also includes (1) being responsible

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[7] Paragraphs .05 and .06 of AS 1201, *Supervision of the Audit Engagement*, describe the nature and extent of supervisory activities necessary for proper supervision of engagement team members.

[8] For audits that involve other auditors, the other auditors are responsible for performing their work with due professional care. The lead auditor's responsibilities for planning the audit and supervising the other auditors' work are set forth in AS 2101, *Audit Planning*, and AS 1201.

[9] *See also* note to AS 1201.05b.

[10] The term "engagement partner," as used in this standard, has the same meaning as defined in Appendix A of AS 1201.

for the appropriate assignment of responsibilities to,[11] and supervision of,[12] engagement team members;[13] (2) determining that the audit is properly planned[14] and performed to obtain reasonable assurance;[15] (3) evaluating that significant findings or issues are appropriately addressed;[16] (4) determining that significant judgments and conclusions on which the auditor's report is based are appropriate and supported by sufficient appropriate audit evidence;[17] and (5) determining that required communications under applicable professional and legal requirements have been made.[18]

.11 Exercising due professional care includes exercising professional skepticism in conducting an audit. Professional skepticism is an attitude that includes a questioning mind and a critical assessment of audit evidence and other information that is obtained to comply with PCAOB standards and rules. The auditor's exercise of professional skepticism includes:

a. Objectively evaluating evidence obtained in an audit (including information that supports and corroborates management's assertions[19] and information that contradicts such assertions), and consideration of the sufficiency and the appropriateness (i.e., relevance and reliability) of that evidence;[20]

b. Remaining alert to conditions that may indicate possible misstatement due to error or fraud;

c. Not being satisfied with evidence that is less than persuasive;

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[11] Paragraph .05 of AS 2301, *The Auditor's Responses to the Risks of Material Misstatement*, establishes requirements regarding the assignment of engagement team members.

[12] *See* AS 1201.

[13] The term "engagement team," as used in this standard, has the same meaning as defined in Appendix A of AS 2101.

[14] *See* AS 2101.03, which describes the engagement partner's responsibility for planning an audit.

[15] *See* paragraph .13 of this standard.

[16] *See* paragraph .12 of AS 1215, *Audit Documentation*.

[17] *See, e.g.*, paragraphs .09-.10 of AS 1220, *Engagement Quality Review*. *See also* AS 2810, *Evaluating Audit Results*.

[18] *See* paragraph .20 of this standard.

[19] *See* AS 1105, *Audit Evidence*, for management's assertions regarding the financial statements and internal control over financial reporting.

[20] *See* AS 1105, which explains what constitutes audit evidence and establishes requirements regarding designing and performing audit procedures to obtain sufficient appropriate audit evidence.

d. Not assuming that management is honest or dishonest; and

e. Considering potential bias on the part of management and the auditor.

## PROFESSIONAL JUDGMENT

.12 The auditor must exercise professional judgment, which involves applying relevant training, knowledge, and experience to make informed decisions and reach well-reasoned conclusions about the courses of action that are appropriate in the circumstances.[21]

Note: Professional judgment is applied in the context of conducting an audit with due professional care in accordance with applicable professional and legal requirements.

## CONDUCTING AN AUDIT

.13 The auditor must plan and perform the audit to obtain sufficient appropriate audit evidence to:

a. Obtain reasonable assurance about whether:

(1) In an audit of financial statements, the financial statements are free of material misstatement,[22] whether due to error or fraud;[23]

(2) In an audit of internal control over financial reporting, material weaknesses exist as of the date specified in management's assessment; and

b. Provide the auditor with a reasonable basis for forming an opinion.[24]

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[21] References to judgment of the auditor in other PCAOB standards have the same meaning as "professional judgment." *See, e.g.*, AS 1215.07 and AS 1220.02.

[22] The term "misstatement," as used in this standard, has the same meaning as defined in Appendix A of AS 2810.

[23] *See* AS 2105, *Consideration of Materiality in Planning and Performing an Audit*, for requirements regarding the auditor's consideration of materiality in planning and performing an audit. *See* AS 2401, *Consideration of Fraud in a Financial Statement Audit*. *See also* paragraph .05 of AS 2405, *Illegal Acts by Clients*.

[24] In circumstances when the auditor is not able to obtain sufficient appropriate audit evidence to provide a reasonable basis for forming an opinion, PCAOB standards require the auditor to disclaim an opinion or withdraw (or resign) from the engagement. *See* AS 3105, *Departures from Unqualified Opinions and Other Reporting Circumstances*, for a financial statement audit and paragraphs .90 through

Note: In an audit of financial statements, the financial statements, including their preparation, are management's responsibility and the auditor's responsibility is to express an opinion on the financial statements. In an audit of internal control over financial reporting, management is responsible for establishing and maintaining effective internal control over financial reporting and for assessing the effectiveness of internal control over financial reporting, and the auditor's responsibility is to express an opinion on the effectiveness of the company's internal control over financial reporting.

.14 Reasonable assurance is not absolute assurance, but a high level of assurance. It is obtained by reducing audit risk to an appropriately low level through the application of due professional care, including by obtaining sufficient appropriate audit evidence.[25] The auditor obtains reasonable assurance that (1) misstatements are detected that, individually or in combination, would result in material misstatement of the financial statements; and (2) in an audit of internal control over financial reporting, material weaknesses are detected.

.15 The auditor must comply with applicable professional and legal requirements in conducting an audit.

Note: When complying with PCAOB standards, the auditor should also take into account PCAOB auditing interpretations[26] applicable to the audit.

.16 The auditor must prepare audit documentation in connection with each engagement conducted in accordance with the standards of the PCAOB.[27] Audit documentation facilitates the planning, performance, and supervision of the engagement and is the basis for reviewing the quality of the work performed in an audit because it provides the engagement partner and other reviewers with written documentation of the evidence supporting the auditor's significant conclusions.[28] AS 1215 also sets forth requirements for the assembly and retention

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.98 of AS 2201, *An Audit of Internal Control Over Financial Reporting That Is Integrated with An Audit of Financial Statements*, and Appendix C of AS 2201, for an audit of internal control over financial reporting.

[25] *See* paragraphs .03-.04 of AS 1101, *Audit Risk*. In a financial statement audit, audit risk is the risk that the auditor expresses an inappropriate audit opinion when the financial statements are materially misstated, *i.e.*, the financial statements are not presented fairly in conformity with the applicable financial reporting framework.

[26] PCAOB auditing interpretations refer to the PCAOB publications entitled "Auditing Interpretations" as currently in effect.

[27] *See, e.g.*, AS 1215; AS 1301, *Communications with Audit Committees*; and AS 3101, *The Auditor's Report on an Audit of Financial Statements When the Auditor Expresses an Unqualified Opinion*.

[28] *See generally* AS 1215.

of audit documentation.[29]

## Auditor Communications

.17 The auditor's report must contain:

a. In an audit of financial statements, an expression of opinion on the financial statements, taken as a whole, or an assertion that an opinion cannot be expressed; and

b. In an audit of internal control over financial reporting, an expression of opinion on the effectiveness of the company's internal control over financial reporting or an assertion that an opinion cannot be expressed.

Note: The auditor's report also contains other elements, such as those included in the basis for opinion or basis for disclaimer of opinion sections, and, if applicable, critical audit matters.[30]

.18 The auditor should express an unqualified opinion only when the auditor has performed the audit in accordance with the standards of the PCAOB and has obtained sufficient appropriate audit evidence to conclude that:

a. In an audit of financial statements, the financial statements, taken as a whole, are presented fairly,[31] in all material respects, in conformity with the applicable financial reporting framework;[32]

b. In an audit of internal control over financial reporting, the company maintained,

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[29] *See* AS 1215.14-.20.

[30] *See* AS 3101 and AS 3105. AS 3101.18 also includes a list of other PCAOB standards with requirements that, in certain circumstances, the auditor include explanatory language (or an explanatory paragraph) in the auditor's report, while not affecting the auditor's opinion on the financial statements. For example, an explanatory paragraph is required when there is substantial doubt about the company's ability to continue as a going concern.

[31] AS 2810.30-.31 describe the auditor's responsibilities related to the evaluation of whether the financial statements are presented fairly, in all material respects, in conformity with the applicable financial reporting framework.

[32] *See* AS 3101 for requirements regarding the content of the auditor's written report when the auditor expresses an unqualified opinion on the financial statements. The auditor should look to the requirements of the SEC for the company under audit with respect to the accounting principles applicable to that company.

in all material respects, effective internal control over financial reporting.[33]

.19 When the auditor conducts an audit in accordance with the standards of the PCAOB, some circumstances require that the auditor depart from an unqualified opinion on the company's financial statements or internal control over financial reporting, and state the reasons for the departure from the unqualified opinion.[34]

.20 The auditor must communicate externally in accordance with applicable professional and legal requirements.[35]

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[33] *See* AS 2201.85-.98 for the form and content of the auditor's report when the auditor conducts an audit of internal control over financial reporting.

[34] *See* AS 3105 for reporting requirements related to departures from unqualified opinions and other reporting circumstances. *See also* AS 2201.90-.98 and Appendix C of AS 2201, for special reporting situations in an audit of internal control over financial reporting.

[35] *See, e.g.*, AS 1301; PCAOB Rule 3211, *Auditor Reporting of Certain Audit Participants*.

## APPENDIX A – Definition

.A1 For purposes of this standard, the term below is defined as follows:

.A2 Applicable professional and legal requirements –

(1) Professional standards, as defined in PCAOB Rule 1001(p)(vi);

(2) Rules of the PCAOB that are not professional standards; and

(3) To the extent related to the obligations and responsibilities of accountants or auditors in the conduct of engagements or in relation to the quality control system, rules of the SEC, other provisions of U.S. federal securities law, ethics laws and regulations, and other applicable statutory, regulatory, and other legal requirements.

# APPENDIX 2 – Amendments to Related PCAOB Auditing Standards

In connection with the adoption of AS 1000, *General Responsibilities of the Auditor in Conducting an Audit* ("AS 1000"), the Board is rescinding certain of its auditing standards and adopting amendments to several related PCAOB auditing standards.

**Auditing Standards Rescinded**

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|---|
| AS 1001, *Responsibilities and Functions of the Independent Auditor* |
| AS 1005, *Independence* |
| AS 1010, *Training and Proficiency of the Independent Auditor* |
| AS 1015, *Due Professional Care in the Performance of Work* |
| AS 2815, *The Meaning of "Present Fairly in Conformity with Generally Accepted Accounting Principles"* |

**Auditing Standards Amended**

| PCAOB Standard | Title | Paragraphs Amended |
|---|---|---|
| AS 1201 | Supervision of the Audit Engagement | .03, .04, .05, .06, and .C4 |
| AS 1215 | Audit Documentation | .02, .03, .06, .06A (new), .07, .11, .12, and .15 |
| AS 2101 | Audit Planning | .03, .07, and .09 |
| AS 2810 | Evaluating Audit Results | .17, .30, .30A (new), and .31 |

## Amendments to AS 1201

I. AS 1201 is amended by adding footnote 1B and deleting footnote 6 to paragraph .03 to read as follows:

.03 The **engagement partner**[1A] is responsible for the engagement and its performance. Accordingly, the engagement partner is responsible for proper supervision of the work of engagement team members[1B] (including engagement team members outside the engagement partner's firm). The engagement partner also is responsible for compliance with PCAOB standards, including standards regarding: using the work of specialists,[2] internal auditors,[4] and others who are involved in testing controls;[5] and dividing responsibility with another accounting firm.[5A] Paragraphs .05–.06 of this standard describe the nature and extent of supervisory activities necessary for proper supervision of engagement team members. Paragraphs .07–.15 of this standard further describe procedures to be performed by the lead auditor with respect

to the supervision of the work of other auditors in conjunction with the required supervisory activities set forth in this standard.[6A]

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[1B] *See also* paragraph .10 of AS 1000, *General Responsibilities of the Auditor in Conducting an Audit*, for an additional description of due professional care as it relates to the engagement partner.

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[6] [Footnote deleted.]

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II. AS 1201 is amended by adding a note to paragraph .04 to read as follows:

.04 The engagement partner may seek assistance from appropriate engagement team members (which may include engagement team members outside the engagement partner's firm) in fulfilling his or her responsibilities pursuant to this standard. Engagement team members who assist the engagement partner with supervision of the work of other engagement team members also should comply with the requirements in this standard with respect to the supervisory responsibilities assigned to them.

Note: When the engagement partner seeks assistance, the engagement partner nevertheless retains primary responsibility for the engagement and its performance. The assistance provided by appropriate engagement team members to supervise, including review, the work of other engagement team members does not replace or reduce the engagement partner's responsibility.

III. AS 1201 is amended by revising footnote 7 of paragraph .05a.; revising the note to paragraph .05b.; and adding Note 1 and Note 2 to paragraph .05c., to read as follows:

.05 The engagement partner and, as applicable, other engagement team members performing supervisory activities, should:

a. Inform engagement team members of their responsibilities,[7] including:

[7] Paragraph .05 of AS 2301, *The Auditor's Responses to the Risks of Material Misstatement*, establishes requirements regarding the appropriate assignment of engagement team members. *See also* AS 1000.10, for an additional description of due professional care as it relates to the engagement partner.

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b. Direct engagement team members to bring significant accounting and auditing issues arising during the audit to the attention of the engagement partner or other engagement team members performing supervisory activities so they can evaluate those issues and determine that appropriate actions are taken in accordance with PCAOB standards;[9]

Note: In applying due professional care in accordance with AS 1000, each engagement team member has a responsibility to bring to the attention of appropriate persons, disagreements or concerns the engagement team member might have with respect to accounting and auditing issues that he or she believes are of significance to the financial statements or the auditor's report regardless of how those disagreements or concerns may have arisen.

c. Review the work of engagement team members to evaluate whether:

(1) The work was performed and documented;

(2) The objectives of the procedures were achieved; and

(3) The results of the work support the conclusions reached.[10]

Note 1: The review and evaluation must be completed prior to the report release date (*see* AS 1215.06 and .15).

Note 2: Notwithstanding assistance from other engagement team members performing supervisory activities, the engagement partner, as the individual primarily responsible for the engagement and its performance, must review documentation sufficient to determine that (i) the engagement was performed as planned; (ii) significant judgments were appropriate and significant findings and issues, along with matters brought to the engagement partner's attention pursuant to paragraph .05b, were appropriately addressed; (iii) the conclusions expressed in the auditor's report are appropriate and supported by sufficient appropriate evidence; and (iv) matters requiring communication under applicable professional and legal requirements are appropriately identified and communicated. The engagement partner's review should include review of documentation of significant findings or issues (see AS 1215.12) and review of documentation required to be reviewed by the engagement quality reviewer pursuant to the requirements of paragraphs .09-.10 and .14-.15 of AS 1220, *Engagement Quality Review*.

IV. AS 1201 is amended by revising footnote 12 to paragraph .06 to read as follows:

.06 To determine the extent of supervision necessary for engagement team members to perform their work as directed and form appropriate conclusions, the engagement partner and other engagement team members performing supervisory activities should take into account:

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d. The knowledge, skill, and ability of each engagement team member.[12]

[12] *See also* AS 2301.05a.

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V. AS 1201 is amended by revising footnote 1 to paragraph .C4 to read as follows:

.C4 Pursuant to paragraph .05a(3) of this standard, the engagement partner and, as applicable, other engagement team members performing supervisory activities should inform the specialist about matters that could affect the specialist's work. This includes, as applicable, information about the company and its environment, the company's processes for developing the related accounting estimate, the company's use of specialists in developing the estimate, relevant requirements of the applicable financial reporting framework, possible accounting and auditing issues, and the need to apply professional skepticism.[1]

[1] *See* paragraph .11 of AS 1000, *General Responsibilities of the Auditor in Conducting an Audit*, for further discussion of the concept of professional skepticism.

## Amendments to AS 1215

VI. AS 1215 is amended by revising paragraph .02 to read as follows:

.02 *Audit documentation* is the written record of the basis for the auditor's conclusions that provides the support for the auditor's representations, whether those representations are contained in the auditor's report or otherwise. Audit documentation also facilitates the planning, performance, and supervision of the engagement, and is the basis for the review of the quality of the work because it provides the reviewer (e.g., engagement partner or other reviewers) with written documentation of the evidence supporting the auditor's significant conclusions. Among other things, audit documentation includes records of 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*.

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VII. AS 1215 is amended by revising paragraph .03 and adding footnote 1B to read as follows:

.03 Audit documentation is reviewed by members of the engagement team[1A] performing the work and might be reviewed by others. Reviewers might include, for example:

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e. Internal and external inspection teams that review documentation to assess audit quality and compliance with applicable professional and legal requirements[1B] and the auditor's own quality control policies and procedures.

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[1B] "Applicable professional and legal requirements" is defined in paragraph .A2 of AS 1000, *General Responsibilities of the Auditor in Conducting and Audit*.

***

VIII. AS 1215 is amended by revising paragraph .06 and adding paragraph .06A to read as follows:

.06 The auditor must document the procedures performed, evidence obtained, and conclusions reached with respect to relevant financial statement assertions.[2] Audit documentation must clearly demonstrate that the work was in fact performed, who performed the work, the person or persons who reviewed the work, and the date of such review. This documentation requirement applies to the work of all those who participate in the engagement as well as to the work of specialists the auditor uses as evidential matter in evaluating relevant financial statement assertions.

.06A 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 or persons who reviewed the work and the date of such review.

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IX. AS 1215 is amended by adding a footnote 2A to paragraph .07 to read as follows (and by revising the numbering of footnotes 2A, 2B, and 2C to paragraph .12 to read as footnotes 2B, 2C, and 2D, respectively):

.07 In determining the nature and extent of the documentation for a financial statement assertion, the auditor should consider the following factors:

- Nature of the auditing procedure;
- Risk of material misstatement associated with the assertion;
- Extent of judgment[2A] required in performing the work and evaluating the results, for example, accounting estimates require greater judgment and commensurately more extensive documentation;

***

[2A] Reference to the judgment of the auditor has the same meaning as "professional judgment" as described in AS 1000.

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X. AS 1215 is amended by revising paragraph .11 to read as follows:

.11 Certain matters, such as auditor independence, staff competence and training, and acceptance and continuance of engagements, may be documented in a central repository for the public accounting firm ("firm") or in the particular office participating in the engagement. If such matters are documented in a central repository, the audit documentation of the engagement should include a reference to the central repository. Documentation of matters specific to a particular engagement should be included in the audit documentation of the pertinent engagement.

XI. AS 1215 is amended by revising paragraph .15 to read as follows:

.15 Prior to the report release date, (i) the auditor must have completed all necessary auditing procedures and obtained sufficient evidence to support the representations in the auditor's report, and (ii) the engagement partner and other engagement team members performing supervisory activities must have completed their reviews of audit documentation. A complete and final set of audit documentation should be assembled for retention (i.e., archived) as of a date not more than 14 days after the report release date (*documentation completion date*). If a report is not issued in connection with an engagement, then the documentation completion date should not be more than 14 days from the date that fieldwork was substantially completed. If the auditor was unable to complete the engagement, then the

documentation completion date should not be more than 14 days from the date the engagement ceased.

## Amendments to AS 2101

XII. AS 2101 is amended by adding a note to paragraph .03 to read as follows:

.03 The **engagement partner**[1] is responsible for the engagement and its performance. Accordingly, the engagement partner is responsible for planning the audit and may seek assistance from appropriate **engagement team** members (which may include engagement team members outside the engagement partner's firm) in fulfilling this responsibility. Engagement team members who assist the engagement partner with audit planning also should comply with the relevant requirements in this standard.

> Note: When the engagement partner seeks assistance, the engagement partner nevertheless retains primary responsibility for the engagement and its performance. The assistance provided by appropriate engagement team members to supervise, including review, the work of other engagement team members does not replace or reduce the engagement partner's responsibility.

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XIII. AS 2101 is amended by adding a footnote 4J to paragraph .07 to read as follows:

.07 The nature and extent of planning activities that are necessary depend on the size and complexity of the company, the auditor's previous experience with the company, and changes in circumstances that occur during the audit. When developing the audit strategy and audit plan, as discussed in paragraphs .08-.10, the auditor should evaluate whether the following matters are important to the company's financial statements and internal control over financial reporting and, if so, how they will affect the auditor's procedures:

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- The auditor's preliminary judgments[4J] about materiality,[5] risk, and, in integrated audits, other factors relating to the determination of material weaknesses;

[4J] Reference to the judgment of the auditor throughout this standard has the same meaning as "professional judgment" as described in AS 1000, *General Responsibilities of the Auditor in Conducting an Audit*.

***

XIV. AS 2101 is amended by revising footnote 10 to paragraph .09 to read as follows:

.09 In establishing the overall audit strategy, the auditor should take into account:

***

d. The nature, timing, and extent of resources necessary to perform the engagement.[10]

[10] *See, e.g.*, paragraph .16 of this standard, and AS 2301.05a.

## Amendments to AS 2810

XV. AS 2810 is amended by adding footnote 9A to paragraph .17 to read as follows:

.17 *Evaluation of the Effect of Uncorrected Misstatements.* The auditor should evaluate whether uncorrected misstatements are material, individually or in combination with other misstatements. In making this evaluation, the auditor should evaluate the misstatements in relation to the specific accounts and disclosures involved and to the financial statements as a whole, taking into account relevant quantitative and qualitative factors.[7] (*See* Appendix B.)

***

Note: As a result of the interaction of quantitative and qualitative considerations in materiality judgments,[9A] uncorrected misstatements of relatively small amounts could have a material effect on the financial statements. For example, an illegal payment of an otherwise immaterial amount could be material if there is a reasonable possibility[10] that it could lead to a material contingent liability or a material loss of revenue.[11] Also, a misstatement made intentionally could be material for qualitative reasons, even if relatively small in amount.

[9A] Reference to the judgment of the auditor throughout this standard has the same meaning as "professional judgment" as described in AS 1000, *General Responsibilities of the Auditor in Conducting an Audit*.

***

XVI. AS 2810 is amended by revising the first Note and adding footnote 17B to paragraph .30 to read as follows:

.30 The auditor must evaluate whether the financial statements are presented fairly, in all material respects, in conformity with the applicable financial reporting framework.[17B]

Note: The applicable financial reporting framework provides the basis for the auditor's judgment regarding the presentation of financial position, results of operations, cash flows, and disclosures in financial statements.

Note: The auditor should look to the requirements of the U.S. Securities and Exchange Commission for the company under audit with respect to the accounting principles applicable to that company.

[17B] AS 2820, *Evaluating Consistency of Financial Statements,* establishes requirements regarding evaluating the consistency of the accounting principles used in financial statements.

XVII. AS 2810 is amended by adding a new paragraph .30A and footnotes 17C and 17D to read as follows:

.30A When evaluating whether the financial statements (including the accompanying notes) present fairly the financial position, results of operations, and cash flows, in all material respects, in conformity with the applicable financial reporting framework, the auditor should evaluate whether:[17C]

a. The financial statements are informative of matters that may affect their use, understanding, and interpretation; and the information in the financial statements is presented and classified appropriately and in a manner that is not misleading;[17D]

b. The accounting principles selected and applied by the company's management are appropriate in the circumstances; and

c. Company transactions and relevant events and conditions are appropriately recognized, measured, and disclosed in the financial statements.

[17C] The concept of materiality is inherent in the auditor's judgment. That concept involves qualitative as well as quantitative factors (*see* AS 2105).

[17D] Regulation S-X Rule 4-01(a), 17 C.F.R. § 210.4-01(a), requires issuers to include in financial statements any further material information as may be necessary to make the required statements, in the light of the circumstances under which they were made, not misleading.

XVIII. AS 2810 is amended by revising and moving footnote 18 and deleting a Note to paragraph .31 to read as follows:

.31 As part of the evaluation of the presentation of the financial statements, the auditor should evaluate whether the financial statements contain the information essential for a fair presentation of the financial statements in conformity with the applicable financial reporting

framework.[18] Evaluation of the information disclosed in the financial statements includes consideration of the form, arrangement, and content of the financial statements (including the accompanying notes), encompassing matters such as the terminology used, the amount of detail given, the classification of items in the statements, and the bases of amounts set forth.

[18] *See* AS 3105.24–.27 for auditor reporting considerations related to inadequate disclosures.

## APPENDIX 3 – Other Amendments to PCAOB Standards

In connection with the adoption of AS 1000, *General Responsibilities of the Auditor in Conducting an Audit*, and related amendments, the Board is adopting conforming amendments to its auditing standards, auditing interpretations, and attestation standards. The table below is a reference tool for the amendments.

**Auditing Standards Amended**

| PCAOB Standard | Title | Paragraph(s) Amended |
|---|---|---|
| AS 1101 | Audit Risk | .03 |
| AS 1105 | Audit Evidence | .B2 |
| AS 1220 | Engagement Quality Review | .02 and .12 |
| AS 2201 | An Audit of Internal Control Over Financial Reporting That Is Integrated with An Audit of Financial Statements | .03, .04, and .09 |
| AS 2301 | The Auditor's Responses to the Risks of Material Misstatement | .05 and .07 |
| AS 2305 | Substantive Analytical Procedures | .09 |
| AS 2315 | Audit Sampling | .02 |
| AS 2401 | Consideration of Fraud in a Financial Statement Audit | .01, .04, .12, and .13 |
| AS 2405 | Illegal Acts by Clients | .05 |
| AS 2410 | Related Parties | .02 |
| AS 2501 | Auditing Accounting Estimates, Including Fair Value Measurements | .27 and .30 |
| AS 2505 | Inquiry of a Client's Lawyer Concerning Litigation, Claims, and Assessments | .13 |
| AS 2601 | Consideration of an Entity's Use of a Service Organization | .32 |
| AS 2605 | Consideration of the Internal Audit Function | .19 |
| AS 2610 | Initial Audits—Communications Between Predecessor and Successor Auditors | .11 |
| AS 2710 | Other Information in Documents Containing Audited Financial Statements | .05 |
| AS 2805 | Management Representations | .02 |
| AS 3101 | The Auditor's Report on an Audit of Financial Statements When the Auditor Expresses an Unqualified Opinion | .01, .02, and .11 |

| PCAOB Standard | Title | Paragraph(s) Amended |
|---|---|---|
| AS 3105 | Departures from Unqualified Opinions and Other Reporting Circumstances | .50 |
| AS 3305 | Special Reports | .03 and .09 |
| AS 4105 | Reviews of Interim Financial Information | .01 and .07 |
| AS 6105 | Reports on the Application of Accounting Principles | .07 and .08 |
| AS 6115 | Reporting on Whether a Previously Reported Material Weakness Continues to Exist | .21 and .38 |
| AI 11 | Using the Work of a Specialist: Auditing Interpretations | .04 |
| AI 18 | Consideration of an Entity's Use of a Service Organization: Auditing Interpretations of AS 2601 | .03 |
| AI 23 | Departures from Unqualified Opinions and Other Reporting Circumstances: Auditing Interpretations of AS 3105 | .06 |
| AI 24 | Special Reports: Auditing Interpretations of AS 3305 | .61 |
| AT No. 1 | Examination Engagements Regarding Compliance Reports of Brokers and Dealers | 6. |
| AT No. 2 | Review Engagements Regarding Exemption Reports of Brokers and Dealers | 5. |
| AT Section 101 | Attest Engagements | .19, .40 and .41 (deleted) |
| AT Section 301 | Financial Forecasts and Projections | .66 |
| AT Section 601 | Compliance Attestation | .31 |
| AT Section 701 | Management's Discussion and Analysis | .29 |

I. AS 1101 is amended by revising footnote 3 to paragraph .03 to read as follows:

.03 To form an appropriate basis for expressing an opinion on the financial statements, the auditor must plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement[2] due to error or fraud. Reasonable assurance[3] is obtained by reducing audit risk to an appropriately low level through applying due professional care, including obtaining sufficient appropriate audit evidence.

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[3] *See* paragraph .14 of AS 1000, *General Responsibilities of the Auditor in Conducting an Audit*, for a discussion of reasonable assurance.

II. AS 1105 is amended by adding footnote 1A to paragraph .B2 to read as follows:

.B2 If in the auditor's judgment[1A] additional evidence is needed, the auditor should perform procedures to gather such evidence. For example, the auditor may conclude that additional evidence is needed because of its concerns about the professional reputation or independence of the investee's auditor, significant differences in fiscal year-ends, significant differences in accounting principles, changes in ownership, changes in conditions affecting the use of the equity method, or the materiality of the investment to the investor's financial position or results of operations. Examples of procedures the auditor may perform are reviewing information in the investor's files that relates to the investee such as investee minutes and budgets and cash flows information about the investee and making inquiries of investor management about the investee's financial results.

[1A] Reference to the judgment of the auditor has the same meaning as "professional judgment" as described in AS 1000, *General Responsibilities of the Auditor in Conducting an Audit*.

III. AS 1220 is amended by adding footnote 1B to paragraph .02 to read as follows:

.02 The objective of the engagement quality reviewer is to perform an evaluation of the significant judgments[1B] made by the engagement team[1A] 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]

[1B] Reference to the judgment of the auditor throughout this standard has the same meaning as "professional judgment" as described in AS 1000, *General Responsibilities of the Auditor in Conducting an Audit*.

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IV. AS 1220 is amended by revising footnote 6 to paragraph .12 to read as follows:

.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.

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[6] *See* AS 1000.09 and .11 for a discussion of the concept of due professional care.

V. AS 2201 is amended by revising footnote 5 to paragraph .03 to read as follows:

.03 The auditor's objective in an audit of internal control over financial reporting is to express an opinion on the effectiveness of the company's internal control over financial reporting. Because a company's internal control cannot be considered effective if one or more material weaknesses exist, to form a basis for expressing an opinion, the auditor must plan and perform the audit to obtain appropriate evidence that is sufficient to obtain reasonable assurance[5] about whether material weaknesses exist as of the date specified in management's assessment. A material weakness in internal control over financial reporting may exist even when financial statements are not materially misstated.

[5] *See* paragraph .14 of AS 1000, *General Responsibilities of the Auditor in Conducting an Audit*, for a discussion of the concept of reasonable assurance in an audit.

VI. AS 2201 is amended by revising paragraph .04 to read as follows:

.04 AS 1000 is applicable to an audit of internal control over financial reporting. That standard requires that the auditor be independent, comply with independence and ethics requirements, be competent, and exercise due professional care, including professional skepticism. This standard establishes the fieldwork and reporting standards applicable to an audit of internal control over financial reporting.

VII. AS 2201 is amended by adding footnote 7B to paragraph .09 to read as follows:

.09 The auditor should properly plan the audit of internal control over financial reporting and properly supervise the engagement team[7A] members. When planning an integrated audit, the auditor should evaluate whether the following matters are important to the company's financial statements and internal control over financial reporting and, if so, how they will affect the auditor's procedures –

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- The auditor's preliminary judgments[7B] about materiality, risk, and other factors relating to the determination of material weaknesses;

[7B] Reference to the judgment of the auditor throughout this standard has the same meaning as "professional judgment" as described in AS 1000.

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VIII. AS 2301 is amended by deleting footnote 1 to paragraph .05a and revising footnote 3 to paragraph .05d to read as follows:

.05 The auditor should design and implement overall responses to address the assessed risks of material misstatement as follows:

a. *Making appropriate assignments of significant engagement responsibilities*. The knowledge, skill, and ability of engagement team[1A] members with significant engagement responsibilities should be commensurate with the assessed risks of material misstatement.

[1] [Footnote deleted.]

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d. *Evaluating the company's selection and application of significant accounting principles*. The auditor should evaluate whether the company's selection and application of significant accounting principles, particularly those related to subjective measurements and complex transactions,[3] are indicative of bias that could lead to material misstatement of the financial statements.

[3] AS 2110.12-.13 discuss the auditor's responsibilities regarding obtaining an understanding of the company's selection and application of accounting principles. *See also* paragraphs .66-.67A of AS 2401, *Consideration of Fraud in a Financial Statement Audit*, and paragraphs .30-.31 of AS 2810, *Evaluating Audit Results*.

IX. AS 2301 is amended by revising footnote 4 to paragraph .07 to read as follows:

.07 Due professional care requires the auditor to exercise professional skepticism.[4] Professional skepticism is an attitude that includes a questioning mind and a critical assessment of the appropriateness and sufficiency of audit evidence. The auditor's responses to the assessed risks of material misstatement, particularly fraud risks, should involve the application of professional skepticism in gathering and evaluating audit evidence.[5] Examples of the application of professional skepticism in response to the assessed fraud risks are (a) modifying the planned audit procedures to obtain more reliable evidence regarding relevant assertions and (b) obtaining sufficient appropriate evidence to corroborate management's explanations or representations concerning important matters, such as through third-party confirmation, use of

a specialist engaged or employed by the auditor,[5A] or examination of documentation from independent sources.

[4] *See* paragraphs .09 and .11 of AS 1000, *General Responsibilities of the Auditor in Conducting an Audit*, for a discussion of due professional care and professional skepticism.

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X. AS 2305 is amended by adding footnote 2 to paragraph .09 to read as follows:

.09 The auditor's reliance on substantive tests to achieve an audit objective related to a particular assertion[1] may be derived from tests of details, from analytical procedures, or from a combination of both. The decision about which procedure or procedures to use to achieve a particular audit objective is based on the auditor's judgment[2] on the expected effectiveness and efficiency of the available procedures. For significant risks of material misstatement, it is unlikely that audit evidence obtained from substantive analytical procedures alone will be sufficient. (See paragraph .11 of AS 2301, *The Auditor's Responses to the Risks of Material Misstatement*.)

[2] Reference to the judgment of the auditor has the same meaning as "professional judgment" as described in AS 1000, *General Responsibilities of the Auditor in Conducting an Audit*.

XI. AS 2315 is amended by adding footnote 2A to paragraph .02 to read as follows:

.02 The auditor often is aware of account balances and transactions that may be more likely to contain misstatements.[2] He considers this knowledge in planning his procedures, including audit sampling. The auditor usually will have no special knowledge about other account balances and transactions that, in his judgment,[2A] will need to be tested to fulfill his audit objectives. Audit sampling is especially useful in these cases.

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[2A] Reference to the judgment of the auditor throughout this standard has the same meaning as "professional judgment" as described in AS 1000, *General Responsibilities of the Auditor in Conducting an Audit*.

XII. AS 2401 is amended by revising paragraph .01 to read as follows:

.01 Paragraph .13 of AS 1000, *General Responsibilities of the Auditor in Conducting an Audit*, requires the auditor to plan and perform the audit to obtain sufficient appropriate audit evidence to obtain reasonable assurance about whether the financial statements are free of

material misstatement whether due to error or fraud.[1] This section establishes requirements and provides direction relevant to fulfilling that responsibility, as it relates to fraud, in an audit of financial statements.[2]

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XIII. AS 2401 is amended by revising paragraph .04 to read as follows:

.04 Although this section focuses on the auditor's consideration of fraud in an audit of financial statements, it is management's responsibility to design and implement programs and controls to prevent, deter, and detect fraud.[3] Management is responsible for adopting sound accounting policies and for establishing and maintaining internal control that will, among other things, initiate, record, process, and report transactions (as well as events and conditions) consistent with management's assertions embodied in the financial statements. Management, along with those who have responsibility for oversight of the financial reporting process (such as the audit committee, board of trustees, board of directors, or the owner in owner-managed entities), should set the proper tone; create and maintain a culture of honesty and high ethical standards; and establish appropriate controls to prevent, deter, and detect fraud. When management and those responsible for the oversight of the financial reporting process fulfill those responsibilities, the opportunities to commit fraud can be reduced significantly.

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XIV. AS 2401 is amended by revising paragraph .12 and footnote 7 to read as follows:

.12 As indicated in paragraph .01, the auditor has a responsibility to plan and perform the audit to obtain sufficient appropriate audit evidence for the auditor to obtain reasonable assurance about whether the financial statements are free of material misstatement, whether due to fraud or error.[7] However, absolute assurance is not attainable and thus even a properly planned and performed audit may not detect a material misstatement resulting from fraud. A material misstatement may not be detected because of the nature of audit evidence or because the characteristics of fraud as discussed above may cause the auditor to rely unknowingly on audit evidence that appears to be valid, but is, in fact, false and fraudulent. Furthermore, audit procedures that are effective for detecting an error may be ineffective for detecting fraud.

[7] For a discussion of the concept of reasonable assurance, *see* AS 1000.14.

XV. AS 2401 is amended by revising paragraph .13 to read as follows:

.13 Due professional care requires the auditor to exercise professional skepticism. *See* AS 1000.09 and .11. Because of the characteristics of fraud, the auditor's exercise of professional skepticism is important when considering the fraud risks. Professional skepticism is an attitude

that includes a questioning mind and a critical assessment of information related to the audit. The auditor should conduct the engagement with a mindset that recognizes the possibility that a material misstatement due to fraud could be present, regardless of any past experience with the entity and regardless of the auditor's belief about management's honesty and integrity. Furthermore, professional skepticism requires an ongoing questioning of whether the information and evidence obtained suggests that a material misstatement due to fraud has occurred. In exercising professional skepticism in gathering and evaluating evidence, the auditor should not be satisfied with less-than-persuasive evidence and avoid assumptions that management is honest or dishonest.

XVI. AS 2405 is amended by revising paragraph .05 to read as follows:

.05 The auditor considers laws and regulations that are generally recognized by auditors to have a direct and material effect on the determination of financial statement amounts. For example, tax laws affect accruals and the amount recognized as expense in the accounting period; applicable laws and regulations may affect the amount of revenue accrued under government contracts. However, the auditor considers such laws or regulations from the perspective of their known relation to audit objectives derived from financial statements assertions rather than from the perspective of legality *per se*. The auditor's responsibility to detect and report misstatements resulting from illegal acts having a direct and material effect on the determination of financial statement amounts is the same as that for misstatements due to error or fraud as described in paragraph .13 of AS 1000, *General Responsibilities of the Auditor in Conducting an Audit*.

XVII. AS 2410 is amended by revising footnote 2 to paragraph .02 to read as follows:

.02 The objective of the auditor is to obtain sufficient appropriate audit evidence to determine whether related parties and relationships and transactions with related parties have been properly identified, accounted for, and disclosed in the financial statements.[2]

[2] *See, e.g.*, paragraphs .30-.31 of AS 2810, *Evaluating Audit Results*.

XVIII. AS 2501 is amended by revising footnote 23 to paragraph .27 to read as follows:

.27 Events and transactions that occur after the measurement date can provide relevant evidence to the extent they reflect conditions at the measurement date.[23]

[23] Evaluating audit evidence from events or transactions occurring after the measurement date, as contemplated in this standard, is a substantive test that differs from the other auditing procedures performed under paragraph .12 of AS 2801, *Subsequent Events*.

XIX. AS 2501 is amended by revising footnote 28 to paragraph .30 to read as follows:

.30 AS 2810 requires the auditor to evaluate the results of audit procedures performed on accounting estimates. This includes:

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d. Evaluating the presentation of the financial statements, including the disclosures and whether the financial statements contain the information essential for a fair presentation of the financial statements in conformity with the applicable financial reporting framework.[28]

[28] *See* AS 2810.30-31.

XX. AS 2505 is amended by revising footnote 7 to paragraph .13 to read as follows:

.13 A lawyer's refusal to furnish the information requested in an inquiry letter either in writing or orally (*see* paragraphs .09 and .10) would be a limitation on the scope of the audit sufficient to preclude an unqualified opinion (*see* paragraphs .05 and .06 of AS 3105, *Departures from Unqualified Opinions and Other Reporting Circumstances*).[7] A lawyer's response to such an inquiry and the procedures set forth in paragraph .05 provide the auditor with sufficient evidential matter to satisfy himself concerning the accounting for and reporting of pending and threatened litigation, claims and assessments. The auditor obtains sufficient evidential matter to satisfy himself concerning reporting for those unasserted claims and assessments required to be disclosed in financial statements from the foregoing procedures and the lawyer's specific acknowledgement of his responsibility to his client in respect of disclosure obligations (*see* paragraph .09*g*). This approach with respect to unasserted claims and assessments is necessitated by the public interest in protecting the confidentiality of lawyer-client communications.

[7] A refusal to respond should be distinguished from an inability to form a conclusion with respect to certain matters of judgment (see paragraph .14). Also, lawyers outside the United States sometimes follow practices at variance with those contemplated by this section to the extent that different procedures from those outlined herein may be necessary. In such circumstances, the auditor should exercise professional judgment in determining whether alternative procedures are adequate to comply with the requirements of this section.

XXI. AS 2601 is amended by adding footnote 2A to paragraph .32 to read as follows:

.32 The service auditor should consider conditions that come to his or her attention that, in the service auditor's judgment,[2A] represent significant deficiencies in the design or operation of the service organization's controls that preclude the service auditor from obtaining reasonable

assurance that specified control objectives would be achieved. The service auditor should also consider whether any other information, irrespective of specified control objectives, has come to his or her attention that causes him or her to conclude (a) that design deficiencies exist that could adversely affect the ability to initiate, record, process, or report financial data to user organizations without error, and (b) that user organizations would not generally be expected to have controls in place to mitigate such design deficiencies.

[2A] Reference to the judgment of the auditor throughout this standard has the same meaning as "professional judgment" as described in AS 1000, *General Responsibilities of the Auditor in Conducting an Audit*.

XXII. AS 2605 is amended by adding footnote 6A to paragraph .19 to read as follows:

.19 The responsibility to report on the financial statements rests solely with the auditor. Unlike the situation in which the auditor divides responsibility for the audit with another public accounting firm,[6] this responsibility cannot be shared with the internal auditors. Because the auditor has the ultimate responsibility to express an opinion on the financial statements, judgments[6A] about assessments of inherent and control risks, the materiality of misstatements, the sufficiency of tests performed, the evaluation of significant accounting estimates, and other matters affecting the auditor's report should always be those of the auditor.

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[6A] Reference to the judgment of the auditor throughout this standard has the same meaning as "professional judgment" as described in AS 1000, *General Responsibilities of the Auditor in Conducting an Audit*.

XXIII. AS 2610 is amended by adding footnote 7A to paragraph .11 to read as follows:

.11 The successor auditor should request that the client authorize the predecessor auditor to allow a review of the predecessor auditor's working papers. The predecessor auditor may wish to request a consent and acknowledgment letter from the client to document this authorization in an effort to reduce misunderstandings about the scope of the communications being authorized.[6] It is customary in such circumstances for the predecessor auditor to make himself or herself available to the successor auditor and make available for review certain of the working papers. The predecessor auditor should determine which working papers are to be made available for review and which may be copied. The predecessor auditor should ordinarily permit the successor auditor to review working papers, including documentation of planning, internal control, audit results, and other matters of continuing accounting and auditing significance, such as the working papers containing an analysis of balance sheet accounts, those relating to contingencies, related parties, and significant unusual transactions. Also, the

predecessor auditor should reach an understanding with the successor auditor as to the use of the working papers.[7] The extent, if any, to which a predecessor auditor permits access to the working papers is a matter of judgment.[7A]

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[7A] Reference to the judgment of the auditor throughout this standard has the same meaning as "professional judgment" as described in AS 1000, *General Responsibilities of the Auditor in Conducting an Audit*.

XXIV. AS 2710 is amended by revising paragraph .05 and adding footnote 3 to paragraph .05 to read as follows:

.05 If, while reading the other information for the reasons set forth in paragraph .04, the auditor becomes aware of information that he believes is a material misstatement of fact that is not a material inconsistency as described in paragraph .04, he should discuss the matter with the client. In connection with this discussion, the auditor should consider that he may not have the expertise to assess the validity of the statement, that there may be no standards by which to assess its presentation, and that there may be valid differences of judgment[3] or opinion between the auditor and client. If the auditor concludes he has a valid basis for concern he should propose that the client consult with some other party whose advice might be useful to the client, such as the client's legal counsel.

[3] Reference to the judgment of the auditor throughout this standard has the same meaning as "professional judgment" as described in AS 1000, *General Responsibilities of the Auditor in Conducting an Audit*.

XXV. AS 2805 is amended by revising footnote 1 to paragraph .02 to read as follows:

.02 During an audit, management makes many representations to the auditor, both oral and written, in response to specific inquiries or through the financial statements. Such representations from management are part of the evidential matter the independent auditor obtains, but they are not a substitute for the application of those auditing procedures necessary to afford a reasonable basis for an opinion regarding the financial statements under audit. Written representations from management ordinarily confirm representations explicitly or implicitly given to the auditor, indicate and document the continuing appropriateness of such representations, and reduce the possibility of misunderstanding concerning the matters that are the subject of the representations.[1]

[1] AS 1000, *General Responsibilities of the Auditor in Conducting an Audit*, describes the auditor's general responsibilities, including the responsibility for exercising professional

skepticism, which includes not being satisfied with evidence that is less than persuasive and not assuming that management is honest or dishonest.

XXVI. AS 3101 is amended by revising paragraph .01, moving footnote 2 to paragraph .01 to paragraph .02, deleting footnote 3 to paragraph .01, and revising footnote 4 to paragraph .02, to read as follows:

.01 This standard establishes requirements regarding the content of the auditor's written report when the auditor expresses an unqualified opinion on the financial statements[1] (the "auditor's unqualified report").

[1] This standard uses the term "financial statements" as used by the U.S. Securities and Exchange Commission ("SEC") to include all notes to the statements and all related schedules. *See* Regulation S-X Rule 1-01(b), 17 C.F.R. 210.1-01(b). This and other PCAOB standards often refer to the notes as disclosures; *see, e.g.*, AS 2110, *Identifying and Assessing Risks of Material Misstatement*.

.02 The auditor is in a position to express an unqualified opinion on the financial statements when the auditor conducted an audit in accordance with the standards of the Public Company Accounting Oversight Board ("PCAOB") and concludes that the financial statements, taken as a whole,[2] are presented fairly, in all material respects,[4] in conformity with the applicable financial reporting framework.[5]

[2] "Taken as a whole" applies equally to a complete set of financial statements and to an individual financial statement with appropriate disclosures.

[3] [Footnote deleted.]

[4] Paragraphs .30-.31 of AS 2810, *Evaluating Audit Results,* describe the auditor's responsibilities related to the evaluation of whether the financial statements are presented fairly, in all material respects, in conformity with the applicable financial reporting framework.

[5] The auditor should look to the requirements of the SEC for the company under audit with respect to the accounting principles applicable to that company.

XXVII. AS 3101 is amended by adding footnote 20B to paragraph .11 to read as follows:

*Determination of Critical Audit Matters*

.11 The auditor must determine whether there are any critical audit matters in the audit of the current period's financial statements. A critical audit matter is any matter arising from the audit of the financial statements that was communicated or required to be communicated to

the audit committee and that: (1) relates to accounts or disclosures that are material to the financial statements and (2) involved especially challenging, subjective, or complex auditor judgment.[20B] Critical audit matters are not a substitute for the auditor's departure from an unqualified opinion (i.e., a qualified opinion, adverse opinion, or disclaimer of opinion on the financial statements as described in AS 3105).

[20B] Reference to the judgment of the auditor throughout this standard has the same meaning as "professional judgment" as described in AS 1000, *General Responsibilities of the Auditor in Conducting an Audit*.

XXVIII. AS 3105 is amended by revising paragraph .50 to read as follows:

.50 During the audit of the current-period financial statements, the auditor should be alert for circumstances or events that affect the prior-period financial statements presented (*see* paragraph .52) or the adequacy of informative disclosures concerning those statements. (*See* AS 2810.30-31.) In updating his or her report on the prior-period financial statements, the auditor should consider the effects of any such circumstances or events coming to his or her attention.

XXIX. AS 3305 is amended by revising paragraph .03 and adding footnote 1A to paragraph .03 to read as follows:

.03 An independent auditor's judgment[1A] concerning the overall presentation of financial statements should be applied within an applicable financial reporting framework (*see* AS 2810, *Evaluating Audit Results*). Normally, the framework is provided by generally accepted accounting principles, and the auditor's judgment in forming an opinion is applied accordingly. In some circumstances, however, a comprehensive basis of accounting other than generally accepted accounting principles may be used.

[1A] Reference to the judgment of the auditor throughout this standard has the same meaning as "professional judgment" as described in AS 1000, *General Responsibilities of the Auditor in Conducting an Audit*.

XXX. AS 3305 is amended by revising paragraph .09 to read as follows:

.09 When reporting on financial statements prepared on a comprehensive basis of accounting other than generally accepted accounting principles, the auditor should consider whether the financial statements (including the accompanying notes) include all informative disclosures that are appropriate for the basis of accounting used. The auditor should apply essentially the same criteria to financial statements prepared on an other comprehensive basis of accounting as he or she does to financial statements prepared in conformity with generally

accepted accounting principles. Therefore, the auditor's opinion should be based on his or her judgment regarding whether the financial statements, including the related notes, are informative of matters that may affect their use, understanding, and interpretation as discussed in AS 2810.30A.

XXXI. AS 4105 is amended by deleting footnote 1A and revising paragraph .01 to read as follows:

.01 The purpose of this section is to establish standards and provide guidance on the nature, timing, and extent of the procedures to be performed by an independent accountant when conducting a review of *interim financial information* (as that term is defined in paragraph .02 of this section). AS 1000, *General Responsibilities of the Auditor in Conducting an Audit*, requires that the auditor be independent, comply with independence and ethics requirements, be competent, and exercise due professional care, including professional skepticism. The same professional qualifications and general principles are applicable to a review of interim financial information conducted in accordance with this section. This section provides guidance on the application of the field work and reporting standards to a review of interim financial information, to the extent those standards are relevant.

XXXII. AS 4105 is amended by adding footnote 5A to paragraph .07 to read as follows:

.07 The objective of a review of *interim financial information* pursuant to this section is to provide the accountant with a basis for communicating whether he or she is aware of any material modifications that should be made to the interim financial information for it to conform with generally accepted accounting principles. The objective of a review of interim financial information differs significantly from that of an audit conducted in accordance with the standards of the PCAOB. A review of interim financial information does not provide a basis for expressing an opinion about whether the financial statements are presented fairly, in all material respects, in conformity with generally accepted accounting principles. A review consists principally of performing analytical procedures and making inquiries of persons responsible for financial and accounting matters, and does not contemplate (a) tests of accounting records through inspection, observation, or confirmation; (b) tests of controls to evaluate their effectiveness; (c) obtaining corroborating evidence in response to inquiries; or (d) performing certain other procedures ordinarily performed in an audit. A review may bring to the accountant's attention significant matters affecting the interim financial information, but it does not provide assurance that the accountant will become aware of all significant matters that would be identified in an audit. Paragraph .22 of this section provides guidance to the accountant if he or she becomes aware of information that leads him or her to believe that the interim financial information may not be in conformity with generally accepted accounting principles. Likewise, the auditor's responsibility as it relates to management's quarterly certifications on internal control over financial reporting is different from the auditor's responsibility as it relates to management's annual assessment of internal control over financial

reporting. The auditor should perform limited procedures quarterly to provide a basis for determining whether he or she has become aware of any material modifications that, in the auditor's judgment,[5A] should be made to the disclosures about changes in internal control over financial reporting in order for the certifications to be accurate and to comply with the requirements of Section 302 of the Act.

[5A] Reference to the judgment of the auditor throughout this standard has the same meaning as "professional judgment" as described in AS 1000.

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XXXIII. AS 6105 is amended by revising paragraph .07 to read as follows:

.07 The reporting accountant should exercise due professional care in performing the engagement and should have the competence to conduct such an engagement. The reporting accountant should also plan the engagement adequately, supervise the work of assistants, if any, and accumulate sufficient information to provide a reasonable basis for the professional judgment described in the report. The reporting accountant should consider the circumstances under which the written report or oral advice is requested, the purpose of the request, and the intended use of the written report or oral advice.

XXXIV. AS 6105 is amended by adding footnote 5A and revising paragraph .08 to read as follows:

.08 To aid in forming a judgment,[5A] the reporting accountant should perform the following procedures: (*a*) obtain an understanding of the form and substance of the transaction(s); (*b*) review applicable accounting principles (*see* AS 2810, *Evaluating Audit Results*); (*c*) if appropriate, consult with other professionals or experts; and (*d*) if appropriate, perform research or other procedures to ascertain and consider the existence of creditable precedents or analogies.

[5A] Reference to the judgment of the auditor throughout this standard has the same meaning as "professional judgment" as described in AS 1000, *General Responsibilities of the Auditor in Conducting an Audit*.

XXXV. AS 6115 is amended by revising paragraph .21 to read as follows:

.21 The engagement to report on whether a previously reported material weakness continues to exist must be performed by an auditor who has the competence as an auditor to conduct such an engagement. In all matters related to the assignment, an independence in mental attitude must be maintained. Due professional care must be exercised in the performance of the engagement and the preparation of the report.

XXXVI. AS 6115 is amended by adding footnote 3A to paragraph .38 to read as follows:

.38 AS 2201.18-.19 should be applied in the context of the engagement to report on whether a previously reported material weakness continues to exist. There may, therefore, be some circumstances in which the scope of the audit procedures to be performed in this engagement will be so limited that using the work of others will not provide any tangible benefit to the company or its auditor. Additionally, the auditor should perform any walkthroughs himself or herself because of the degree of judgment[3A] required in performing this work.

[3A] Reference to the judgment of the auditor throughout this standard has the same meaning as "professional judgment" as described in AS 1000, *General Responsibilities of the Auditor in Conducting an Audit*.

XXXVII. AI 11 is amended by adding footnote 3A to paragraph .04 to read as follows:

.04 *Interpretation*—During the audit, an auditor may encounter complex or subjective matters potentially material to the financial statements. Such matters may require special skill or knowledge and in the auditor's judgment[3A] require using the work of a specialist to obtain appropriate evidential matter.

[3A] Reference to the judgment of the auditor throughout this interpretation has the same meaning as "professional judgment" as described in AS 1000, *General Responsibilities of the Auditor in Conducting an Audit*.

XXXVIII. AI 18 is amended by adding footnote 1A to paragraph .03 to read as follows:

.03 In describing the nature, timing, and extent of the tests applied, the service auditor also should indicate whether the items tested represent a sample or all of the items in the population, but need not indicate the size of the population. In describing the results of the tests, the service auditor should include exceptions and other information that in the service auditor's judgment[1A] could be relevant to user auditors. Such exceptions and other information should be included for each control objective, whether or not the service auditor concludes that the control objective has been achieved. When exceptions that could be relevant to user auditors are noted, the description also should include the following information:

[1A] Reference to the judgment of the auditor throughout this interpretation has the same meaning as "professional judgment" as described in AS 1000, *General Responsibilities of the Auditor in Conducting an Audit*.

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XXXIX. AI 23 is amended by adding footnote 1C to paragraph .06 to read as follows:

.06 Thus, the auditor would examine the outside firm's program, observe its procedures and controls, make or observe some physical counts of the inventory, recompute calculations of the submitted inventory on a test basis and apply appropriate tests to the intervening transactions. The independent auditor ordinarily may reduce the extent of the work on the physical count of inventory because of the work of an outside inventory firm, but any restriction on the auditor's judgment[1C] concerning the extent of his or her contact with the inventory would be a scope restriction.

[1C] Reference to the judgment of the auditor throughout this interpretation has the same meaning as "professional judgment" as described in AS 1000, *General Responsibilities of the Auditor in Conducting an Audit*.

XL. AI 24 is amended by adding footnote 12 and revising paragraph .61 to read as follows:

.61 *Interpretation*—Financial statements prepared on a statutory basis are financial statements prepared on a comprehensive basis of accounting other than GAAP according to AS 3305.04. AS 3305.09 states that "When reporting on financial statements prepared on a comprehensive basis of accounting other than generally accepted accounting principles, the auditor should consider whether the financial statements (including the accompanying notes) include all informative disclosures that are appropriate for the basis of accounting used. The auditor should apply essentially the same criteria to financial statements prepared on an other comprehensive basis of accounting as those applied to financial statements prepared in conformity with generally accepted accounting principles. Therefore, the auditor's opinion should be based on his or her judgment[12] regarding whether the financial statements, including the related notes, are informative of matters that may affect their use, understanding, and interpretation as discussed in paragraphs .30A-.31 of AS 2810, *Evaluating Audit Results*.

[12] Reference to the judgment of the auditor throughout this interpretation has the same meaning as "professional judgment" as described in AS 1000, *General Responsibilities of the Auditor in Conducting an Audit*.

XLI. Attestation Standard No. 1 is amended by revising paragraph 6 to read as follows:

6. An auditor who performs an examination engagement pursuant to this standard must:

a. Have competence in attestation engagements;[10A]

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d. Exercise due professional care, including the application of professional skepticism,[11/] in planning and performing the examination and the preparation of the report.

Note: Due professional care imposes a responsibility on each engagement team[11A/] member to comply with this standard. The exercise of due professional care requires critical review at every level of supervision of the work done and the judgment[11B/] exercised by those assisting in the engagement, including preparing the report. Due professional care concerns what the auditor does and how well the auditor does it. Due professional care means acting with reasonable care and diligence; exercising professional skepticism; acting with integrity; and complying with applicable professional and legal requirements.[11C/]

[10A/] *See* paragraph .07 of AS 1000, *General Responsibilities of the Auditor in Conducting an Audit*, for a description of competence.

[11/] Professional skepticism is an attitude that includes a questioning mind and a critical assessment of audit evidence and other information that is obtained to comply with PCAOB standards and rules. *See* paragraph .11 of AS 1000 for further discussion of the concept of professional skepticism.

[11A/] The term "engagement team," as used in this standard for examination engagements, has a meaning analogous to the term's definition in Appendix A of AS 2101, *Audit Planning*, for audit engagements.

[11B/] Reference to the judgment of the practitioner throughout this standard has the same meaning as "professional judgment" as described in AS 1000.

[11C/] The term "applicable professional and legal requirements," as used in this standard, has the same meaning as defined in Appendix A of AS 1000, which includes professional standards as defined in PCAOB Rule 1001(p)(vi) (i.e., certain accounting principles and other standards) and rules of the PCAOB that are not professional standards. This definition also includes statutes with which the auditor is required to comply. *See, e.g.*, Section 10A of the Securities Exchange Act of 1934, 15 U.S.C. § 78j-1.

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XLII. Attestation Standard No. 2 is amended by revising paragraph 5 to read as follows:

5. An auditor who performs a review engagement must:

a. Have competence in attestation engagements;[7A/]

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d. Exercise due professional care, including the application of professional skepticism,[8/] in planning and performing the review and preparation of the report.

Note: Due professional care imposes a responsibility on each engagement team[8A/] member to comply with this standard. The exercise of due professional care requires critical review at every level of supervision of the work done and the judgment[8B/] exercised by those assisting in the engagement, including preparing the report. Due professional care concerns what the auditor does and how well the auditor does it. Due professional care means acting with reasonable care and diligence; exercising professional skepticism; acting with integrity; and complying with applicable professional and legal requirements.[8C/]

[7A/] *See* paragraph .07 of AS 1000, *General Responsibilities of the Auditor in Conducting an Audit*, for a description of competence.

[8/] Professional skepticism is an attitude that includes a questioning mind and a critical assessment of audit evidence and other information that is obtained to comply with PCAOB standards and rules. *See* paragraph .11 of AS 1000 for further discussion of the concept of professional skepticism.

[8A/] The term "engagement team," as used in this standard for review engagements, has a meaning analogous to the term's definition in Appendix A of AS 2101, *Audit Planning*, for audit engagements.

[8B/] Reference to the judgment of the practitioner throughout this standard has the same meaning as "professional judgment" as described in AS 1000.

[8C/] The term "applicable professional and legal requirements," as used in this standard, has the same meaning as defined in of Appendix A of AS 1000, which includes professional standards as defined in PCAOB Rule 1001(p)(vi) (i.e., certain accounting principles and other standards) and rules of the PCAOB that are not professional standards. This definition also includes statutes with which the auditor is required to comply. *See, e.g.*, Section 10A of the Securities Exchange Act of 1934, 15 U.S.C. § 78j-1.

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XLIII. AT 101 is amended by revising paragraphs .19 to read as follows:

.19 The first general standard is—The engagement shall be performed by a practitioner having competence in the attest function.[fn 6]

[fn 6] *See* paragraph .07 of AS 1000, *General Responsibilities of the Auditor in Conducting an Audit*, for a description of competence.

XLIV. AT Section 101 is amended by revising paragraph .40 and adding footnote 7A and footnote 7B to read as follows:

.40 Due professional care concerns what the practitioner does and how well the practitioner does it. Due professional care means acting with reasonable care and diligence; exercising professional skepticism;[fn 7A] acting with integrity; and complying with applicable professional and legal requirements.[fn 7B] The exercise of due professional care requires critical review at every level of supervision of the work done and the judgment exercised by those assisting in the engagement, including the preparation of the report.

[fn 7A] Professional skepticism is an attitude that includes a questioning mind and a critical assessment of information related to the audit. *See* paragraph .11 of AS 1000 for further discussion of the concept of professional skepticism.

[fn 7B] The term "applicable professional and legal requirements," as used in this standard, has the same meaning as defined in Appendix A of AS 1000, which includes professional standards as defined in PCAOB Rule 1001(p)(vi) (i.e., certain accounting principles and other standards) and rules of the PCAOB that are not professional standards. This definition also includes statutes with which the auditor is required to comply. *See, e.g.*, Section 10A of the Securities Exchange Act of 1934, 15 U.S.C. § 78j-1.

XLV. AT Section 101 is amended by deleting paragraph .41 and footnote 8:

[.41] [Paragraph deleted.]

[fn 8] [Footnote deleted.]

XLVI. AT Section 301 is amended by adding footnote 30 to paragraph .66 to read as follows:

.66 If, after discussing the matter as described in paragraph .65, the practitioner concludes that a material misstatement of fact remains, the action he or she takes will depend on his or her judgment [fn 30] in the particular circumstances. The practitioner should consider steps such as

notifying the responsible party in writing of his or her views concerning the information and consulting his or her legal counsel about further appropriate action in the circumstances.

[fn 30] Reference to the judgment of the practitioner throughout this standard has the same meaning as "professional judgment" as described in AS 1000, *General Responsibilities of the Auditor in Conducting an Audit*.

XLVII. AT Section 601 is amended by adding footnote 8A to paragraph .31 to read as follows:

.31 In an engagement to examine compliance with specified requirements, the practitioner seeks to obtain reasonable assurance that the entity complied, in all material respects, based on the specified criteria. This includes designing the examination to detect both intentional and unintentional material noncompliance. Absolute assurance is not attainable because of factors such as the need for judgment, [fn 8A] the use of sampling, and the inherent limitations of internal control over compliance and because much of the evidence available to the practitioner is persuasive rather than conclusive in nature. Also, procedures that are effective for detecting noncompliance that is unintentional may be ineffective for detecting noncompliance that is intentional and concealed through collusion between personnel of the entity and a third party or among management or employees of the entity. Therefore, the subsequent discovery that material noncompliance exists does not, in and of itself, evidence inadequate planning, performance, or judgment on the part of the practitioner.

[fn 8A] Reference to the judgment of the practitioner throughout this standard has the same meaning as "professional judgment" as described in AS 1000, *General Responsibilities of the Auditor in Conducting an Audit*.

XLVIII. AT Section 701 is amended by adding footnote 17A to paragraph .29 to read as follows:

.29 In an engagement to examine MD&A, the practitioner plans and performs the examination to obtain reasonable assurance of detecting both intentional and unintentional misstatements that are material to the MD&A presentation taken as a whole. Absolute assurance is not attainable because of factors such as the need for judgment [fn 17A] regarding the areas to be tested and the nature, timing, and extent of tests to be performed; the concept of selective testing of the data; and the inherent limitations of the controls applicable to the preparation of MD&A. The practitioner exercises professional judgment in assessing the significant determinations made by management as to the relevancy of information to be included, and the estimates and assumptions that affect reported information. As a result of these factors, in the great majority of cases, the practitioner has to rely on evidence that is persuasive rather than convincing. Also, procedures may be ineffective for detecting an intentional misstatement that is concealed through collusion among client personnel and third parties or among management or employees of the client. Therefore, the subsequent discovery

that a material misstatement exists in the MD&A does not, in and of itself, evidence (a) failure to obtain reasonable assurance; (b) inadequate planning, performance, or judgment on the part of the practitioner; (c) the absence of due professional care; or (d) a failure to comply with this section.

fn 17A Reference to the judgment of the practitioner throughout this standard has the same meaning as "professional judgment" as described in AS 1000, *General Responsibilities of the Auditor in Conducting an Audit*.