Securities Regulation Daily Wrap Up, ACCOUNTING AND AUDITING —PCAOB amends auditing standards on lead auditor's use of other auditors, (Jun. 21, 2022)

Securities Regulation Daily Wrap Up

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The new requirements include a mix of principles and rules to address audit deficiencies and weaknesses that have been observed in audits involving multiple auditors.

The Public Company Accounting Oversight Board (PCAOB) adopted amendments to its auditing standards as well as a new standard to strengthen requirements for audits involving multiple audit firms. The new requirements are designed to improve audit coordination and communication when several accounting firms or individual accountants perform important work on an audit (*Planning and Supervision of Audits Involving Other Auditors and Dividing Responsibility for the Audit with Another Accounting Firm*, June 21, 2022).

"Today, after an extensive process of analysis and public input regarding the lead auditor's use of other auditors, the Board is taking action to improve audit quality and strengthen investor protection," said PCAOB Chair Erica Y. Williams. "These amendments will require audit firms to ensure that lead auditors sufficiently plan, supervise, and evaluate the work of other auditors."

This was the first standard setting recommendation considered by the newly constituted Board. The PCAOB considered three rounds of comments relating to proposed lead auditor requirements in 2016, 2017, and 2021.

Need for requirements. As Chair Erika Williams explained, the use of other auditors has become more prevalent as companies continue to increase their global presence. The use of multiple auditors can result in miscommunication or misunderstandings about the nature, timing, and extent of the other auditor's procedures. In turn, this can cause audit quality to suffer.

Although some audit firms have improved their approach to supervising the work of other auditors, the PCAOB continues to see enforcement cases and inspection deficiencies that point to failures by certain lead auditors overseeing the work of other auditors, said Williams.

New requirements. The changes provide the following requirements:

- The engagement partner must determine whether his or her firm's participation in the audit is sufficient for the firm to carry out the responsibilities of a lead auditor and report as such. The amendments provide considerations for the engagement partner in making the determination and require that the audit's engagement quality reviewer review the determination.
- When determining the engagement's compliance with independence and ethics requirements, the lead auditor must understand the other auditors' knowledge of those requirements and experience in applying them. The lead auditor must obtain and review written affirmations regarding the other auditors' policies and procedures related to those requirements and regarding compliance with the requirements, and a description of certain auditor-client relationships related to independence. The amendments also require information to be shared about changes in circumstances and for affirmations and descriptions to be updated in light of those changes.
- The lead auditor must understand the knowledge, skill, and ability of other auditors' engagement team members who assist the lead auditor with planning and supervision, and obtain a written affirmation from other auditors that their engagement team members possess the knowledge, skill, and ability to perform assigned tasks.

- The lead auditor must supervise other auditors under the Board's standard on audit supervision and inform other auditors about the scope of their work, identified risks of material misstatement, and certain other key matters. The lead auditor and other auditors must communicate about the audit procedures to be performed, and any changes needed to the procedures. In addition, the amendments require the lead auditor to obtain and review written affirmations from other auditors about their performance of work in accordance with the lead auditor's instructions, and to direct other auditors to provide certain documentation about their work.
- In multi-tiered audits, a first other auditor may assist the lead auditor in performing certain required procedures with respect to second other auditors.

New standard for divided audits. In infrequent situations, the lead auditor divides responsibility for a portion of the audit with another audit firm and therefore does not supervise the work performed by that firm. In these situations, the lead auditor refers in the audit report to the work of that auditor (i.e., a referred-to auditor).

For these situations, the rulemaking rescinds an interim standard but carries forward and strengthens some of its requirements in a new standard. The new standard requires that the lead auditor determine that audit procedures were performed regarding the consolidation or combination of financial statements of the business units audited by the referred-to auditor into the company's financial statements.

The standard also requires that the lead auditor obtain the referred-to auditor's written representation that it is independent and duly licensed to practice. Finally, the lead auditor must disclose in the audit report the magnitude of the portion of the financial statements and, if applicable, internal controls audited by the referred-to auditor.

Board member statements. The Board voted unanimously to adopt the new final requirements. In addition to Chair Williams, Board Members Christina Ho, Duane DesParte, Kara Stein, and Anthony Thompson issued statements in support of the requirements.

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