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Accounting and Auditing Manual/1977

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Chapter 4400

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Review

4401 General Standards

4401.01 *Applicability*

Every engagement, regardless of its nature or size, is subject to review. The review procedures that relate primarily to accounting and reporting matters are discussed in this chapter. Review procedures applicable to other services rendered by the firm are described at Chapter 6300, *Tax Manual*, and Chapter 7800, *Management Advisory Services Manual*.

4401.02 *Responsibilities*

Independent review procedures are an integral part of applying due professional care, and their importance cannot be overemphasized.

Responsibility for an engagement extends to every person who contributes to the final result. Because of the nature of our services, errors of principle or detail may enter into the work at any point. For this reason, each engagement is reviewed carefully, and each level of review is recorded in the work papers.

Certain engagements entail a statutory legal liability that exceeds an accountant's liability under common law. Other engagements may involve special reporting considerations. Ordinarily, such engagements require additional administrative and review procedures. See Appendix C for an index of approval and notification requirements, Section 3405 for notification procedures, and Section 4406 for technical review procedures.

4401.03 *Levels of Review—Audit Engagements*

The review process for audit engagements is a related interdependent process with five distinct levels of responsibility as follows:

1. In-charge accountant
2. Account administrator
3. Review department
4. Tax department
5. Post-review

Each function has its distinct purpose, and the person performing the review should not be comforted by the fact that his work will in turn be reviewed. Specific responsibilities that must be completed at each level of review before a report is released are described in Sections 4402 through 4405.

For unaudited financial statements, the levels of review differ somewhat. See Section 3809.

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4401.04 Evidence of Review

Evidence of audit work paper review is provided by signing Index 1100—Work Paper Review of the *Guide to Audit Objectives and Procedures* and by initials or signatures, as appropriate, on individual *Audit Guide* modules and work papers.

Evidence of work paper review for unaudited financial statement engagements is provided by signing the appropriate confidential engagement programs and initialing work papers. See Section 3802.

Evidence of report review is provided by signing the "Report Guide Sheet" (Form 1-311).

4401.05 Review Questionnaires

Review questionnaires tend to duplicate procedures in engagement programs. For example, such questionnaires may ask whether confirmations were obtained or inventories observed when the same questions are posed in the engagement program. Consequently, it is the firm's policy not to use review questionnaires.

4401.06 Final Reading and Signing of Report

All financial statements are finally read and interchecked by the review partner or his delegate. All audit report letters are signed by the review partner or another partner.

4401.07 Disposal of Nonevidential Matter

During the course of an engagement, certain nonevidential matter is accumulated. This includes "to do" lists, open questions, point sheets, superseded work papers, and reviewers' notes. At the conclusion of all review procedures, the work papers must be complete and in support of the report, and all nonevidential matter shall be destroyed. Any matters of continuing significance should be incorporated in a memorandum to the account administrator. See Section 3502.04—Data for Subsequent Year.

4401.08 Approval and Notification Requirements

Certain matters require clearance or notification of such parties as the regional director of accounting and auditing, firm counsel in the National office, assistant national managing partner-technical, and the regional managing partner. Such matters are indexed in Appendix C.

Ordinarily, clearances should be evidenced by an appropriate interoffice memorandum prepared by the review department and addressed to the regional director of accounting and auditing.

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4402 In-charge Accountant**4402.01 General**

The responsibilities of the in-charge accountant are set forth in Section 3205. His responsibility includes the adequacy of the work of all personnel assisting in the engagement.

Concurrent reviewing by the in-charge accountant takes place continuously throughout the field work as a part of supervision and training. However, such review is not a substitute for performing the procedures in this section before submitting the report and work papers for review by the account administrator.

4402.02 Work Papers and Permanent Files

The in-charge accountant enters his signature on Index 1100—Work Paper Review of the *Guide to Audit Objectives and Procedures* only after being satisfied that all work paper review comments developed during this level of review have been disposed of (including appropriate revisions of the work papers) and the audit documentation is, to the best of the in-charge accountant's knowledge and belief, complete.

In performing the work paper review, the in-charge accountant:

- Determines that the scope of work defined in the respective sections of the *Guide to Audit Objectives and Procedures* (or such other audit program as may be applicable in the circumstances) has been carried out and that any significant matters or problems noted have been properly considered, resolved, and documented.
- Determines that adequate audit evidence has been obtained to provide a reasonable basis for the auditor's report letter in observance of the generally accepted auditing standards of field work.
- Determines that all phases of the work have been concluded in accordance with the engagement plan and the work papers completed in accordance with Chapter 3500.
- Reviews each lead schedule and related *Audit Guide* module, commentaries, and supporting analyses and initials and dates all work papers prepared by others.
- Initials and dates the trial balance, lead schedules, and commentaries and dates and signs the final procedure in each *Audit Guide* module, indicating that the audit objectives for each segment of the audit were met and that significant factors considered in meeting the objectives were summarized in the appropriate sections of the work papers.
- Resolves all points and questions raised in the work papers.

Review

- Determines that the work papers contain only information related to the specific engagement and that all nonevidential matter has been disposed of.
- Reviews all journal entries to see that they have been properly prepared.
- Obtains the account administrator's approval of the journal entries (preferably before leaving the field) before submitting them to the client for approval.
- Obtains the account administrator's approval that the field work is in fact complete.
- Evaluates the performance of those assisting in the conduct of the field work.

4402.03 *Financial Statements and Auditors' Report*

The "Report Guide Sheet" (Form 1-311) is prepared by the in-charge accountant. After he is satisfied that all report review comments developed during his review have been disposed of, and the financial statements and auditors' report letter are in conformity with professional standards and the firm's policies and procedures, the in-charge accountant signs the report review section of the "Report Guide Sheet."

4403 Account Administrator

4403.01 *General*

The account administrator conducts a review of the engagement as part of his ultimate responsibility for each of the firm's clients assigned to him. His intimate knowledge of the client's affairs provides him with an informed basis for appraising the adequacy of procedures and the adherence to proper accounting principles. His review also alerts him to pertinent matters relating to his overall consulting activities with the client.

The account administrator's review is a continuing matter not restricted to the period immediately following the field work phase of the engagement. It is imperative that he periodically visit the client's offices during the course of the engagement to review progress and to determine that all questions raised have been satisfactorily resolved.

Only in rare instances is it anticipated that an account administrator will delegate his review function to another individual. In such cases, it may only be delegated to a partner or manager who is familiar with the account. However, in all instances, the account administrator remains responsible for such review and should ascertain that the review has been properly performed before the work papers and report are forwarded to the review department.

Review

The degree of detail in which the account administrator's review is performed depends on various factors pertinent to the circumstances of the engagement and will be influenced by the degree of reliance which he can place on the staff executing the assignment and the degree to which there was a preliminary review. However, the account administrator is *not* responsible for such review procedures as tracing figures and mechanical accuracy; the responsibility for these procedures rests with the review department.

Where feasible, the account administrator review takes place in the field during the final stages of the audit. This permits the account administrator to more easily resolve any questions which arise and permits him to extend audit procedures if that appears necessary.

4403.02 *Work Papers and Permanent Files*

The account administrator enters his signature on Index 1100—Work Paper Review of the *Guide to Audit Objectives and Procedures* only after being satisfied that all work paper and permanent file review comments developed during this level of review have been disposed of (including appropriate revisions of the work papers) and the audit documentation is complete.

In performing the work paper review, the account administrator:

- Reads the trial balance, lead schedules, individual modules of the *Guide to Audit Objectives and Procedures*, and commentaries to determine that generally accepted auditing standards have been employed, paying particular attention to:
 - Evidence that the scope of work approved by the account administrator and defined in the respective sections of the *Audit Guide* (or such other audit program as may be applicable in the circumstances) has been carried out by the in-charge accountant.
 - Documentation that significant matters or problems noted have been properly considered and resolved.
- Determines the adequacy of explanations for substantial variances between current and prior year financial statement balances.
- Reads supporting analyses and permanent file data, giving particular attention to:
 - Sufficiency of competent evidential matter in support of our report letter, specifically considering confirmations, representations, minutes, contracts, leases, loan agreements, and similar documents.

Review

- Documentation of planning, execution of the engagement, including control and budgeting of time.
- Completeness of audit memorandums and commentaries, with specific emphasis on content, as outlined in Section 3501.04.
- Approves journal entries (preferably in the field) before they are submitted to the client for approval.
- Resolves all questions raised in the review performed by the in-charge accountant.
- Initials key work papers as follows:
 - Initials and dates the trial balance, lead schedules, the "Reviewed By" box on the first page of each *Audit Guide* module, and commentaries, indicating that the audit objectives for each segment of the audit were met and that significant factors considered in meeting the objectives were summarized in the appropriate sections of the work papers.
 - Initials and dates selected other work papers that he deems necessary, especially those where his intimate knowledge of the client's affairs is particularly applicable.
- Evaluates the performance of the in-charge accountant and assistants in the conduct of the engagement.

4403.03 *Financial Statements and Auditors' Report*

The account administrator signs the report review section of the "Report Guide Sheet" after being satisfied that all report review comments developed during his review have been disposed of and the financial statements and auditors' report letter are in conformity with professional standards and the firm's policies and procedures.

In performing the financial statement and auditors' report letter review, the account administrator:

- Analyzes the financial statements and notes to make certain that representations and amounts in the report make sense from a business standpoint.
- Reads the complete report to determine that generally accepted auditing standards have been employed, giving particular attention to:
 - Presentation of financial statements in accordance with generally accepted principles of accounting that have been consistently observed.
 - Disclosures necessary for a fair presentation of the financial statements have been made by the client.

Review

The account administrator is also responsible for reviewing the report with the client after it has been approved by the review department.

4403.04 *Other Information Relating to Auditors' Report*

The account administrator determines that documents containing our auditors' report have been reviewed to ascertain that they do not contain comments or representations that are misstatements of fact or are materially inconsistent with the financial statements on which we have rendered our opinion. Review should be made of such documents as drafts of annual reports and printers' proofs of the president's letter. If there appear to be inconsistencies or misstatements, the matter is discussed with the client to determine our course of action. If the client refuses to comply with our request, the account administrator should immediately notify the regional director of accounting and auditing. (See Section 3735.)

4404 *Review Department*4404.01 *Impartial Review of Audit Engagements*

It is the policy of the firm to require an impartial review of each audit engagement by an individual unrelated to the engagement or the client. This function is performed in each office by the person designated as the review partner or his delegate.

4404.02 *Report Letter Signatures*

All reports are finally read and interchecked by the review partner or his delegate. All audit report letters are signed by the review partner or another partner.

4404.03 *One-Partner Offices*

In one-partner offices the managing partner is responsible for the review function. If there is a regularly assigned reviewer other than the managing partner in such office, then the following procedures apply:

- For engagements where the account administrator is the managing partner, the regularly assigned reviewer of the office will perform the review department review, since the managing partner is responsible for performing the account administrator review on the engagements for which he is the account administrator.
- All reports are finally read, interchecked, and signed by the managing partner.

In one-partner offices where there is no regularly assigned reviewer other than the managing partner, the following procedures apply:

- The managing partner personally performs the review department review on all audited financial statements engagements except those on which he is the account administrator.
- For the review department review of those engagements where the managing partner is the account administrator, such review must be performed by the review department of the nearest separate office; the regional director of accounting and auditing approves the office selected for the review.
- The managing partner or the review partner of the reviewing office finally reads and signs all reports.

4404.04 *Engagements Involving More Than One Office*

Ordinarily, the operating office that performs the work is responsible for conducting all levels of review in conformity with Sections 4402 through 4405. This applies to engagements involving a division, subsidiary, or other segment of a business where the overall engagement is under the primary control of another operating office. However, the controlling or principal office may assume full responsibility for performing the tax department review (Section 4405) and review department review (Section 4404) and in such cases should notify the offices involved of the decision.

When all levels of review are performed by the operating office that conducted the engagement, the principal operating office should read the work papers, permanent file, and report (if any) to determine whether there are matters that may affect the consolidating or combining of accounts in the financial statements, financial statement disclosures, or audit procedures applicable to the entire engagement.

If the work for another office consists of observation of inventories, counting petty cash, or other procedures not constituting a complete audit of an entity, the principal office ordinarily assumes the review responsibility for such work.

4404.05 *Responsibilities Shared with Tax Department*

Income taxes are generally material in relation to the financial statements. Because of the complexities of the tax laws and their effect on current professional pronouncements, the tax and review departments share the responsibility for approving income tax amounts and disclosures in financial statements. Accordingly, it is essential that these two departments coordinate their respective reviews to assure that the objectives of the impartial review are met. Moreover, it is important to have a clear understanding of the differences between treatment of items in

the determination of pretax accounting income and of taxable income. Only by such understanding can there be a correct classification between the taxes estimated to be payable and the tax effects of timing differences and operating losses that are the components of income tax expense. This understanding should be in advance of the time at which the financial results will be cleared, so as to avoid last-minute changes in both income statement and balance sheet accounts.

Each department is expected to have a sufficient knowledge of accounting for income taxes to meet the firm's objectives for review of the income tax accruals and related expenses.

4404.06 *Approval of Work Papers and Permanent Files*

The review department reviewer enters his signature on Index 1100—Work Paper Review of the *Guide to Audit Objectives and Procedures* only after being satisfied that all work paper and permanent file review comments developed during this level of review have been disposed of (including appropriate revisions of the work papers), and the audit documentation is, to the best of the reviewer's belief, complete.

4404.07 *Approval of Financial Statements and Auditors' Report*

The review department reviewer signs the report review section of the "Report Guide Sheet" after being satisfied that all report review comments developed during his review have been disposed of and the financial statements and auditors' report letter are in conformity with the professional standards and the firm's policies and procedures. Before signing, the reviewer should ascertain that all hold items have been properly recorded on the "Report Guide Sheet"; it is the responsibility of the partner or manager signing for final release on the "Report Guide Sheet" to ascertain that all hold items have been cleared. The review department should consider withholding signature for its review on the "Report Guide Sheet" whenever a hold item involves a matter that could materially change the financial statements or auditors' report letter.

4404.08 *Acceptance for Review*

Frequently, the review department performs a cursory review upon receipt of a report draft and related files to determine whether, on its face, it appears to be acceptable for review department review. If there are obvious omissions, the engagement is returned to the account administrator for completion. If the engagement appears complete, the engagement is scheduled for review department review.

Review

4404.09 *Review Procedures*

The steps set forth on the Standard Review Department Procedures at Section 4404.10 will be performed as a *minimum* review by a review department for audit engagements.

The review of audited financial statement engagements requires the exercise of judgment. Accordingly, a reviewer should expand the scope of his review beyond the standard procedures to the extent he feels necessary in the circumstances.

The review partner is responsible for closely supervising the work of the review department. The degree of supervision depends on the qualifications and experience of the reviewers and the tasks to which they are assigned on certain engagements. The review partner may assign certain phases of the review department review procedures, outlined in Section 4404.10, to various members of the review staff. In the case of certain mechanical accuracy test procedures, persons outside the department may be delegated mechanical steps 1-4 of Section 4404.10 only, provided that all of the requirements for review department are met. If the review department is satisfied that such mechanical accuracy steps have been effectively performed, it need not also perform them. Nevertheless, the review department remains responsible for assuring that the mechanical accuracy procedures are performed.

4404.10 *Standard Review Department Procedures*

Overall objectives. The overall objectives of the review department review of audit engagements are to determine that the work papers and financial statements, standing alone, demonstrate and document compliance with:

- Generally accepted auditing standards.
- Generally accepted accounting principles.
- Policies and procedures of the firm as set forth in its manuals.

Mechanical accuracy. The objective of the mechanical accuracy review is to assure the mechanical and arithmetical accuracy of the report and related work papers. Some calculations involve analyses of complex agreements and judgments about the applicability of certain provisions. In such cases, the calculation should be tested as part of the audit verification reviews.

The mechanical accuracy review includes:

1. Tracing amounts that arrive at account balances to lead schedules. (For example, Work Paper Index 6310 to Work Paper Index 6300.)
2. Tracing lead schedules to working trial balances. (For example, Work Paper Index 6300 to Work Paper Index 1402.)

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3. Tracing all figures in report to work papers.
4. Interchecking all figures in report to work papers.
5. Test-checking important calculations in the work papers, such as:
 - Accruals for interest income and expense.
 - Accruals and provisions for state and federal income taxes.
 - Accruals for pension and profit-sharing plans.
 - Accrued bonuses.
 - Depreciation (if the original calculation was made by us).
 - Inventory price testing (if adjustments result therefrom).
 - Installment sale income.
6. Checking in detail certain calculations. Among these are:
 - Earnings per share.
 - Compliance with loan agreement restrictions.
 - Loose figures for footnotes.

Administration and control. The objectives of the administrative control review are to evaluate compliance with the firm's policies and procedures for assembling evidential matter necessary to support the representation stated in our auditors' report letter.

Factors to consider in evaluating compliance include:

- Preparation of financial statements in conformity with the formats set forth in Chapter 4700.
- Clearance of accounting and reporting matters with the regional office, as listed at Appendix C.
- Supervision, administration, and control of the engagement.
- Organization, indexing, and content of work papers and permanent files, in conformity with Chapter 3500.
- Filing, tailoring, cross-referencing, and signing the *Guide to Audit Objectives and Procedures* in conformity with Section 3502.03.
- Completion of tax grouping sheets and income tax returns prior to receipt of the engagement for review, in conformity with Section 3505.03.
- Assembly of footnote data in the work papers at Index 1600.
- Completeness of the permanent file.
- Use of audit techniques, such as statistical sampling, AUDASSIST, and flow charting.

Review

- Use of flow charts, portraying our understanding of the accounting policies and procedures, prepared in cases:
 - Where the accounting policies and procedures were sufficiently intricate to require flow charting to gain an understanding of the system.
 - Where the audit approach placed greater reliance on the accounting system (including tests of compliance with the accounting procedures—see *AICPA Professional Standards*, AU Section 320.55) in determining the nature, timing, or extent of substantive tests (see *AICPA Professional Standards*, AU Sections 320.69–90) of particular classes of transactions or balances.
 - Where the engagement required a report on “compliance,” that is, determining whether certain regulations or contractual agreements were met. (See *AICPA Professional Standards*, AU Sections 640–641.)

Audit verification. The objectives of the audit verification review are to:

- Determine whether the scope of work defined in the respective sections of the audit program has been carried out and that any significant matters or problems noted have been properly considered and resolved.
- Determine whether adequate audit evidence has been obtained to provide a reasonable basis for the auditors’ report letter.

Consider the following factors in evaluating whether the audit objectives have been met.

- Nature and timing of verification procedures
- Scope of work
 - Period covered
 - Size and definition of field
 - Salient factors tested
 - Sample selection method
 - Number of items tested
- Quality of corroborating evidential matter examined
- Clarity of work performed
- Resolution of questions
- Adequacy of commentaries

In the conduct of the review department review, the reviewer should consider the following key areas of audit verification:

Review

- Proper treatment of areas that may lead to, or are susceptible to, material misstatement of the financial report. Adequacy of account administrator’s review of such areas and consideration of the peculiarities of the client and its industry during the review.
- Relevance of commentaries describing the characteristics of the accounting policies and procedures that affect the nature, timing, and extent of audit procedures to be applied in the examination of the financial statements.
- Selection of the standard audit procedures outlined in the *Guide to Audit Objectives and Procedures* (or such other audit program applicable in the circumstances) that pertain to the engagement and modifications that are necessitated by changes in the client’s business practices and accounting policies and procedures.
- Adequacy of explanations of material variations between current and prior year financial statement amounts.
- Completeness of representation letters.
- Propriety of reporting and disclosure of transactions with related parties.
- Adequacy of support for and accuracy of all material journal entries prepared by us.
- Factors that may have a bearing on amounts reported in the balance sheet, such as:
 - Results of accounts receivable verification by confirmation and supplementary procedures.
 - Adequacy of allowance for doubtful accounts.
 - Adequacy of inventory verifications, including validity of conclusions as to price testing, physical inventory observations, and factors relating to possible obsolescence. Reliability of confirmations of inventory held for and by third parties. Conformity of cost accounting procedures to generally accepted accounting principles. Proper use and documentation of “lower cost or market.”
 - Valuation of investments.
 - Adequacy of examination of property, plant, and equipment accounts.
 - Valuation and amortization of intangibles.
 - Realizability of assets at carrying amounts.
 - Scope, basis of selection, and results of liability verification.
 - Adequacy of accrued liabilities.

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- Adequacy of provision for income taxes. (See Section 4404.05.)
- Adequacy of verification procedures on long-term debt, including confirmations and review of indenture restrictions.
- Adequacy of examination of capital accounts.
- Factors that may have a bearing on the results of operations, such as:
 - Proper period for reporting of income and expense.
 - Significant aspects of business practices for sales, costs, and expenses, and the accounting methods employed, including current year changes that may affect the engagement.
 - Accounting policies and procedures for the sales/accounts receivable/cash receipts functions, the purchases/accounts payable/cash disbursements functions, and the payroll functions that may affect the nature, timing, and extent of audit procedures applied.
 - Adequacy of the tests of the applicable books and records.
 - a) General journal
 - b) Sales journal
 - c) Cash receipts books
 - d) Accounts receivable subsidiary ledger
 - e) Inventory records
 - f) Cash sales journal
 - g) Purchases
 - h) Accounts payable
 - i) Cash disbursements
 - j) Payroll journal
 - k) Payroll labor cost distribution
 - Adequacy of the tests of the underlying documents.
 - a) Sales invoices
 - b) Customer orders
 - c) Shipping documents
 - d) Credit memos
 - e) Purchase orders
 - f) Vouchers
 - g) Vendors' invoices
 - h) Cancelled checks
 - i) Wage rate authorization
 - j) Time cards
 - Adequacy of the tests of other income and expense accounts.

Financial statements and auditors' report review. The objectives of the financial statements and auditors' report review are to:

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- Determine whether management's representations in the financial statements as to the company's financial position, results of operations, and changes in financial position are in agreement or reconciled with the company's records.
- Determine whether the individual items comprising the financial statements are properly classified and described and that they are satisfactorily grouped to avoid showing unnecessary detail.
- Determine that our report letter is appropriate in the circumstances.

Factors to consider in evaluating whether the audit objectives have been met include:

- Report terminology, content, and presentation conform to standards set forth in Chapter 4700.
- Our report letter complies with Chapter 3900 and with the AICPA statements on auditing standards.
- Accounting principles conform to opinions, statements, and interpretations of the body designated by the AICPA to establish such pronouncements.
- Completeness of footnote disclosures. See Section 4715—Notes to Financial Statements.
- Reports on companies filing with regulatory agencies conform to the *SEC Guide*.

Concluding the review. In concluding his review, the reviewer does the following:

- Clears all questions with the account administrator. Controversial points that cannot be resolved between the review partner and account administrator are referred to the managing partner for decision.
- Communicates any suggested changes in our report letter or the financial statements to the account administrator. The reviewer should ordinarily not make the changes himself.
- Communicates suggestions (in addition to those developed by the in-charge accountant) for the following year to the account administrator. Such suggestions would typically include statistical sampling, assistance of client's personnel to prepare schedules, use of computer audit specialists and AUDASSIST, and possible reduction of test scope.
- If necessary, requests review partner to communicate comments about adequacy of in-charge accountant review and the account administrator review to managing partner.

- Ascertains that all hold items have been properly recorded on the "Report Guide Sheet." (It is the responsibility of the partner or manager signing for final release on the "Report Guide Sheet" to ascertain that all hold items have been cleared. The review department should consider withholding signature for detailed review on the "Report Guide Sheet" whenever a hold item involves a matter that could materially change the report.)
- Signs Index 1100 of the work papers as reviewer.
- Signs the "Report Guide Sheet" as reviewer.

4405 Tax Department

4405.01 *General*

Income taxes are generally material in relation to the financial statements. Accordingly, it is the policy of the firm to require tax department approval of tax accruals prior to the release of audited and certain unaudited financial statements. Therefore, the tax department reviews (preferably in the field) each client's income tax accruals and related expenses. (See also Section 3809.01 with respect to unaudited financial statements.)

4405.02 *Responsibilities and Procedures*

Section 6308 of the *Tax Manual* states the tax accrual review policies applicable to the tax department. The following subjects are included:

- Review policy
- Concurrent review of tax accrual and tax returns
- Cursory review
- Consultation with audit staff
- Responsibilities shared with review department (see Section 4404.05)
- Approval of work papers and permanent files
- Approval of financial statements and report letter
- Review procedures

4405.03 *Tax Return Review*

The tax department's review of tax returns is discussed in the *Tax Manual*.

4406 Technical Reviews

4406.01 *General*

The account administrator has the primary responsibility for each of his assigned clients, and therefore reviews the work papers and all audit reports related to the client prior to issuance.

4405

In conducting their respective reviews, the in-charge and the account administrator perform such procedures as they deem necessary to fulfill the objectives of Sections 4402 and 4403.

4406.02 *Applicability of Technical Review Policy*

The review policies discussed in this section apply to the following:

- All registration statements under the Securities Act of 1933, such as Forms S-1, S-8, S-11, and S-14, including posteffective amendments thereto.
- Applications for exemption under Regulation A.
- Registration statements on Form 10 under the Securities Exchange Act of 1934.
- Proxy statements involving business combinations.
- Sale or acquisition audits where financial statements with which we are associated may be relied upon by the buyer and/or seller.
- Audits of broker-dealers and broker-dealer stock exchange questionnaires.
- Blue sky filings containing financial statements with which our name is associated.
- Private offering circulars containing financial statements with which our name is associated.
- Foreign securities offerings that include financial statements with which our name is associated.
- Reports pursuant to the Investment Advisers Act of 1940.
- Local government securities offerings.

Refer to Sections 3405 and 4401.08 for notification requirements.

In addition to the foregoing situations, regional directors of accounting and auditing are authorized to require technical reviews on a case-by-case basis in such situations as they deem appropriate.

4406.03 *Reports Not Covered by Technical Review Policy*

Specifically not covered by the technical review policy are current, quarterly, and annual reports filed with the SEC. However, if a publicly held client is planning to file a registration statement for the sale of additional securities or as a posteffective amendment because of outstanding warrants or employee stock options, the annual report on Form 10-K should be subjected to these review policies prior to its filing.

*Review***4406.04 Responsibilities of the Technical Reviewer**

The primary function of the technical reviewer is to assure the quality of our work, both as to compliance with the rules and regulations of the regulatory agency and the essential quality of the underlying audit. The role of the technical reviewer encompasses the following goals, and his effort should be directed specifically toward their accomplishment.

- To make high-level technical experience available to all offices and account administrators on an as-needed basis.
- To enhance the firm's reputation on technical accounting matters in the eyes of the SEC and the entire financial community.
- To protect the other partners of the firm from the substantial liability that can be incurred in connection with these engagements.
- To minimize the costs to our clients in connection with these technical engagements by bringing in additional skills and experience at an early point in the engagement.

The technical reviewer is expected to remain abreast of current developments in regulatory areas. In this connection, individuals interested in assuming this role should so direct their reading and professional development courses. The individual who assumes the responsibility of a technical reviewer is required to make himself available to consult with the account administrator in connection with any client problems for which he has assumed responsibility and to keep in close contact with the regional director with respect to problems and policy questions that arise in connection with the engagement.

It is the function of the technical reviewer to give each engagement to which he is assigned a careful, critical, and impartial review. The technical reviewer must be fully aware of the responsibility which he has undertaken to protect the interests of the firm.

The technical reviewer should determine the scope and the extent of the review that he feels are appropriate after consultation with the regional director of accounting and auditing. In situations where the engagement involves an established client that has been filing regularly with an exchange, the technical reviewer may make the decision to limit the scope of his review. But, where an initial filing is involved, and particularly in situations involving companies in the development stage, the technical reviewer may wish to review the audit work papers and underlying documents and undertake such other review procedures as he feels will best fulfill his responsibilities. The extent to which the technical reviewer examines work papers and underlying documents rests in his discretion.

Review

The technical reviewer's role is that of a detached final reviewer. Generally, his review should not be conducted in the client's office; his review is essentially an internal matter and should be handled away from the pressures of client situations.

The technical reviewer should remain in close touch with the account administrator during the field work phase of the engagement until the engagement is completed and should be prepared to make himself available for consultation as required. He should give final approval of comfort letters and participate in the selection of the individuals who can best represent the firm in attending due-diligence meetings, meetings with the SEC, and the consideration of key questions.

The technical reviewer should keep the regional director informed of progress and important matters and should inform the regional director, the director of quality control—National office, and the account administrator of the completion of the assignment by use of the "Technical Review Notification" form (see Section 3405.54).

4406.05 Responsibilities of the Account Administrator

The account administrator has primary responsibility for the conduct of the engagement. He is responsible for the conduct of the audit, meeting deadlines, maintaining client contact, and dealing with all essential client and staff-oriented problems. The details of the account administrator's usual responsibilities are discussed at Section 3200. The account administrator's review of each engagement for which he is responsible is discussed in detail at Section 4403.

In working with the technical reviewer, the account administrator has certain important obligations to the technical reviewer. It must be kept in mind that the technical reviewer is frequently a partner from another office who has client responsibilities comparable to those of the account administrator. In assuming the review responsibility, he has agreed to make himself available on matters not involving his clients for an unpredictable amount of time. Therefore, it is imperative that the account administrator be sensitive to this situation and advise the technical reviewer well in advance of all unusual problems or questions involved in the engagement. He should keep the technical reviewer informed about the anticipated timing of the entire engagement and the time that will be required of the technical reviewer. In addition, it is generally helpful if the account administrator provides the technical reviewer with copies of old reports, registration statements, and other data that will be helpful in acquainting the reviewer with the client's operations and problems. He should also undertake to keep the technical reviewer advised of all current developments during the progress of the engagement. Finally, it is the responsibility of the account administrator to see that copies of drafts, proofs, and the related

material are received by the technical reviewer, as well as by the director of quality control—National office and the regional director of accounting and auditing.

4406.06 *Delegation*

The technical reviewer may not delegate his *responsibility* to any other person. However, he may delegate a portion of his review on a particular assignment to another person who is subject to his direct administration and control. Ordinarily, the decision to delegate should be discussed with the regional director of accounting and auditing.

4410 *Unaudited Financial Statements*

See Section 3809 for a discussion of review policies and procedures applicable to unaudited financial statements.

4411 *Limited Purpose Reports*

Limited purpose reports containing incomplete financial presentations are subject to the same review procedures as reports containing full financial statements. Letters containing incomplete financial presentations come within the firm's definition of limited purpose reports and must be reviewed as though they were formal reports. See Chapters 4000 and 4200.

4420 *Review by Others*

4420.01 *General*

The retention of work papers is necessary to protect the firm's position in the event of subsequent inquiry. Generally, the work papers are the only evidence of work performed by the firm. While the rules in the following section apply particularly to reviews conducted by other accounting firms, they are equally applicable to others, such as attorneys or actuaries. See Section 3504, Work Papers—Control.

Procedures to be followed in the event that a partner or employee of the firm is served with a subpoena to testify or to produce records are set out at Section 1603 of the *Administrative Manual*.

4420.02 *Successor Accountants*

The firm's policy in those cases involving an examination of our work papers by other accounting firms is that upon receiving instructions in writing from the client or former client, we will permit such examination, subject to the following conditions:

- The review can only be conducted with the approval of the account administrator and managing partner.

- The examination must be made in our offices during regular working hours.
- A representative of our firm must always be present during the review.
- No papers may be removed from our office under any circumstances.
- All fees due the firm must be paid before any examination of work papers is permitted.

Frequently, successor accountants request copies of our permanent file and work paper data. As a general rule, we do not allow the successor firm to copy our audit programs (e.g., *Guide to Audit Procedures and Objectives*) and work paper conclusions. Ordinarily, we allow the successor accountant to copy work papers containing accounting information of continuing significance, such as work papers supporting balance sheet accounts and those applicable to contingencies.

4420.03 *Successor Auditors*

It is also the policy of our firm to comply with AU Section 315 of *AICPA Professional Standards* concerning communications with successor auditors. Our conduct is similar to the policy described in Section 4420.02. However, the following conditions are also applicable:

- Ordinarily, we will be available to consult with the successor auditor and allow him to review our work papers.
- There should be agreement as to which work papers are to be reviewed and which are to be copied.
- We should limit our consultation and work paper review to the successor auditor who has accepted the engagement (unless we have made suitable fee arrangements with the client).
- When the account administrator and managing partner conclude that, for certain reasons, they are unwilling to permit the review of our work papers, concurrence of the regional director of accounting and auditing must be obtained.

4420.04 *Governmental Agencies*

When governmental agencies request access to our work papers, the firm permits such inspection only on written authorization of the client or in response to a subpoena. In the event that work papers are subpoenaed, either by a governmental agency or in connection with civil litigation, the regional director of accounting and auditing and the firm counsel in the National office are immediately notified. In addition, any work papers that are subpoenaed by governmental agencies must be microfilmed or photocopied before such papers are released from our possession.

Review

It is the policy of the firm to cooperate with revenue agents conducting routine examinations of income tax returns filed by our clients. Generally, work papers are not volunteered to the revenue agent, and those submitted to the agent are limited in scope to the particular question raised. In all instances, we insist that the papers be made available only upon written authorization of the client or in response to a subpoena. (See Section 6404 of the *Tax Manual* for policies related to the examination of work papers by the Internal Revenue Service.)

4421 Regional Director Review**4421.01 Post-review of Reports**

Copies of certain reports are required to be sent to regional offices. See Section 4305.01 for details. Such reports are postreviewed on a test basis in the regional offices.

Significant comments or suggestions are forwarded to the local office review department and the responsible account administrators. Account administrators should take appropriate action to correct deficiencies that are called to their attention.

4421.02 Review of Correspondence

Correspondence relating to auditing or accounting matters is reviewed by the regional directors of accounting and auditing. If deemed necessary, comments or suggestions are issued to the operating office.

4422 Audit Standards Review

Audit standards reviews of operating offices are conducted annually.

Such reviews are conducted by audit standards team leaders assisted by partners, managers, and other selected personnel from offices other than that under review.

For further details of audit standards reviews, refer to the *Audit Standards Team Leader Guide*.

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