



STAFF INSPECTION BRIEF

The staff of the Public Company Accounting Oversight Board (“PCAOB” or “Board”) prepares Inspection Briefs to assist auditors, audit committees, investors, and preparers in understanding the PCAOB inspection process and its results. The statements contained in Staff Inspection Briefs do not establish rules of the Board or constitute determinations of the Board and have not been approved by the Board.

Information about 2015 Inspections of Auditors of Brokers and Dealers

The PCAOB Division of Registration and Inspections has prepared this Inspection Brief to provide information about its inspections in 2015 of auditors of brokers and dealers registered with the Securities and Exchange Commission (“SEC” or the “Commission”) related to their audits of brokers and dealers, and to highlight important aspects of the inspection objectives, plan, and scope. It is intended to assist auditors, audit committees, investors, and preparers in further understanding the inspection process and its results.

Under the interim inspection program,¹ the Board conducts inspections of registered public accounting firms in connection with their performance of audits, issuance of audit reports, and related matters involving brokers and dealers registered with the Commission² to assess compliance with the professional standards, rules of the Commission and the Board, and the Sarbanes-Oxley Act of 2002 (the “Act”).

The interim inspection program also helps to inform the Board’s eventual determinations about the scope and elements of a permanent inspection program, including whether and how to differentiate among classes of brokers and dealers, whether to exempt any categories of registered public accounting firms, and the establishment of minimum inspection frequency schedules.

1 On June 14, 2011, the Board adopted Rule 4020T to establish an interim inspection program related to the audits of brokers and dealers. See PCAOB Release No. 2011-001 (June 14, 2011). The SEC approved this rule on August 18, 2011. See Exchange Act Release No. 65163 (August 18, 2011).

2 Under Section 15 of the Securities Exchange Act of 1934 (“Exchange Act”), most brokers and dealers must register with the SEC and join a self-regulatory organization, such as the Financial Industry Regulatory Authority (“FINRA”). Hereinafter, the use of the terms “broker(s) and dealer(s)” or “broker(s) or dealer(s)” refers to brokers and dealers registered with the SEC.

In 2015, Inspections staff is evaluating how firms performed on audit and attestation engagements and is focusing on:

- Financial statement audit areas that had deficiencies identified in past inspections, including revenue recognition and use of information produced or used by brokers or dealers,
- The examination of compliance reports and the review of exemption reports under newly applicable PCAOB standards,
- Audit procedures on the supplemental schedules to the financial statements,
- The engagement quality review, and
- Auditor independence.

Interim Inspection Program for Auditors of Brokers and Dealers

Overview of the Inspection Plan and Scope

The inspections during 2015 of 75 firms that audit brokers and dealers are expected to cover certain portions of approximately 115 selected audit and attestation engagements of brokers and dealers.

The audit and attestation engagements of brokers and dealers are now required to be conducted in accordance with PCAOB standards as a result of amendments to Exchange Act Rule 17a-5 (“Rule 17a-5”) that became effective for broker and dealer

annual reports with fiscal years ended on or after June 1, 2014.

Inspections staff is focusing on areas relevant to the amendments to Rule 17a-5 and on other areas that are unique to audits and other engagements conducted pursuant to PCAOB standards. Inspections staff is also focusing on areas with noted observations from past inspections, as described in the various reports on the progress of the interim inspection program that are available on the PCAOB website.³

On an annual basis, the results of the inspections are stratified by certain audit firm characteristics, and broker and dealer characteristics to determine whether there are any discernible relationships. Characteristics of audit firms have included the number of broker or dealer audits performed by the firm and whether the firm also audited issuers. Characteristics of brokers and dealers have included reported actual net capital as referenced in Exchange Act Rule 15c3-1 (“Rule 15c3-1”)

2015 Inspections by the Numbers*



75 firms

that audit brokers and dealers and portions of



115 audits

*Numbers are approximate

³ For more information related to the progress of the interim inspection program refer to <http://pcaobus.org/Inspections/Pages/PublicReports.aspx>.

and whether the broker or dealer maintained a Customer Reserve Bank Account, as referenced in Exchange Act Rule 15c3-3 (“Rule 15c3-3”).

Because certain areas of focus are selected for all inspected audit and attestation engagements, the selections as a whole are less risk weighted when compared to the Board’s issuer inspection programs. Additional focus areas may be selected on a risk-weighted basis, however, with risk in this context being the risk to customers of the broker or dealer.

In addition to reviewing certain portions of selected audit work performed by firms, inspection procedures may include obtaining an understanding of how certain aspects of a firm’s quality control system apply to its audit and attestation engagements of brokers and dealers, with particular emphasis on the transition to the PCAOB’s standards.

Key Areas of Inspection Focus

Inspections staff is assessing how auditors complied with PCAOB standards. Certain areas of focus include:

Audit deficiencies in the financial statement audit

Inspections staff considers deficiencies cited in previous interim inspection program progress reports and evaluates how an audit firm has performed in those areas. Certain areas of focus with recurring deficiencies include:

Revenue recognition

Inspections staff considers the firm’s assessed risks of misstatement at the relevant assertion level, including fraud risk assessment, and the firm’s response to those assessed risks, including tests of details where required by PCAOB standards. In addition, inspectors are assessing procedures to evaluate incomplete or omitted disclosures and presentation of revenue in the financial statements.

Use of information produced or used by brokers or dealers

Firms frequently use as audit evidence, information produced by the broker or dealer or produced by a service organization and used by the broker or dealer in maintaining its books and records. Inspections staff is assessing audit procedures performed to evaluate the accuracy, completeness, and whether the information is sufficiently precise for the purposes of the audit.



Inspections Focus

- Audit deficiencies in the financial statement audit
- Attestation standards
- Auditing supplemental information accompanying audited financial statements
- Engagement quality review
- Auditor independence

Attestation standards

PCAOB Attestation Standard No. 1, *Examination Engagements Regarding Compliance Reports of Brokers and Dealers*, establishes the requirements for auditor examination of certain statements in the compliance reports of brokers and dealers.

Inspection focus includes examination procedures performed:

- To determine whether brokers or dealers maintained effective internal control over compliance with financial responsibility rules⁴ for the period covered by the broker's or dealer's statement and as of fiscal year end, and
- Regarding statements by the broker or dealer regarding its compliance with Rule 15c3-1 and Rule 15c3-3(e), as of fiscal year end.

PCAOB Attestation Standard No. 2, *Review Engagements Regarding Exemption Reports of Brokers and Dealers*, establishes the requirements for auditor review of the statements in the exemption reports of brokers and dealers. Inspection focus includes review

procedures performed to identify exceptions to the exemption provisions of Rule 15c3-3 and assessment of risk factors associated with exemption compliance.

Auditing supplemental information accompanying audited financial statements

PCAOB Auditing Standard No. 17 establishes the auditor's responsibilities with respect to supplemental information required to accompany the financial statements, including the supplemental schedules required by SEC rule to accompany the broker's or dealer's financial statements. Inspections staff is focusing on the auditor's materiality considerations with respect to the supplemental information, procedures to test the accuracy and completeness of the information, and the auditor's evaluation of whether the supplemental information complies with relevant SEC rules.

Engagement quality review

Inspections staff is assessing the engagement quality review process as applied to the financial statement audit and attestation engagements.

⁴ See footnote 10 in PCAOB Attestation Standard No. 1.

Auditor independence

Inspections staff is focusing on firm compliance with applicable independence requirements,⁵ including the prohibition against providing bookkeeping or other services related to the accounting records or financial statements that will be subject to audit procedures by the firm.⁶ Inspections staff has frequently observed apparent violations of these requirements during PCAOB inspections of the firms that audit brokers and dealers. In addition, the PCAOB has issued settled orders imposing disciplinary sanctions against 14 audit firms for independence violations when auditing brokers and dealers.⁷

Additional Information

The Board publishes a progress report on the interim inspection program every 12 months, which includes a discussion of inspection observations. Observations from the planned 2015 inspections will be covered in an annual report to be issued in 2016. Observations from inspections completed in 2014 are covered in the annual report issued in August of 2015.

In addition to webcasts and podcasts of PCAOB open board meetings and webinars,⁸ the PCAOB conducts forums around the country for auditors of brokers and dealers that provide information about the Board, the interim inspection program, observations from the interim inspection program, and audit and attestation engagements of brokers and dealers.⁹

5 Rule 17a-5(f)(1) requires auditors to be independent of their broker-dealer audit clients in accordance with Rule 2-01 of Regulation S-X (other than the provisions relating to partner rotation, compensation, audit committee pre-approval, and employment-related cooling-off periods, which apply only to issuer audits). PCAOB Rule 3520, *Auditor Independence* requires registered firms and associated persons to be independent of the audit client, including satisfying the SEC's independence criteria and any other applicable independence criteria. Certain additional independence criteria applicable to audits of brokers and dealers are set out in PCAOB Rule 3521, *Contingent Fees*, and PCAOB Rule 3522, *Tax Transactions*. The independence criteria in PCAOB Rule 3523, *Tax Services for Persons in Financial Reporting Oversight Roles*, apply by their terms only to audits of issuers and do not apply to audits of brokers and dealers.

6 See Rule 2-01(c)(4)(i) of Regulation S-X.

7 For more information on the settled disciplinary orders refer to http://pcaobus.org/News/Releases/Pages/07092015_Enforcement.aspx and http://pcaobus.org/News/Releases/Pages/12082014_Enforcement.aspx.

In addition, the SEC settled actions for violations of independence rules against eight audit firms, which were not the same firms as those that reached settlements with the Board.

8 Additional information relating to inspections of brokers and dealers can be found in webcasts and podcasts of PCAOB open board meetings and webinars. See <http://pcaobus.org/News/Webcasts/Pages/default.aspx>.

9 For more information on 2015 forums for auditors of brokers and dealers refer to http://pcaobus.org/News/Releases/Pages/2015_BDF_Announcement.aspx.

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