

# Executive Highlights

## Annual Report on the Interim Inspection Program Related to Audits of Brokers and Dealers

This Executive Highlights of the Public Company Accounting Oversight Board's [Annual Report on the Interim Inspection Program Related to Audits of Brokers and Dealers](#), issued on August 20, 2018 (the "Annual Report"), provides actions for audit firms, 2017 inspection results, and considerations for broker-dealer owners and audit committees (or equivalent). The following are important takeaways based on inspection results described in the Annual Report:

- Auditors should focus on improving their quality control systems to perform high quality audits and attestation engagements.
- Overall deficiencies remained high, although inspectors found fewer independence violations than in past years.
- Broker-dealer owners and audit committees (or equivalent) are encouraged to discuss these results with their auditors.

Auditors of broker-dealers should read the Annual Report to better understand the areas where inspections found deficiencies and evaluate their programs and procedures to prevent similar deficiencies and improve audit quality. In addition, the Annual Report can help inform broker-dealer owners and audit committees (or equivalent) when overseeing the work of their auditors.

## Actions for Audit Firms

Firms that audit broker-dealers should focus their efforts on improving their quality control systems and their performance in the areas described below.

### Improving Quality Control Systems

Quality control systems should be continually reassessed for effectiveness and improved in order to perform high quality audits and attestation engagements. Examples of improvements include:

#### Addressing Identified Deficiencies

- Enhancing, maintaining, and monitoring policies and procedures in order for the audit firm to be independent
- Determining that a qualified reviewer performs an engagement quality review for all audits and attestation engagements
- Emphasizing the importance of appropriate supervision, including review, to partners and supervisory staff

## Strengthening Control Systems

- Accepting only the audits and attestation engagements that can be performed with professional competence
- Enhancing, maintaining, and monitoring policies and procedures in order for the work to meet PCAOB standards and rules
- Applying effective root cause analyses to deficiencies
- Training audit firm staff on the importance of performing work with due professional care, including professional skepticism

## Performing Audits and Attestation Engagements

The areas covered in the 2017 inspections were based on risk and the significance to the audits and attestation engagements. The five areas with the highest percentage of deficiencies are listed below with examples of the deficient procedures:

### Auditing Revenue

- Performing sufficient risk assessment procedures for auditing revenue that include understanding the broker-dealer's products and sources of revenue, internal control over financial reporting, and process for executing transactions
- Testing important controls to support the audit firm's intended reliance on controls to reduce its substantive testing
- Testing material classes of revenue to address the risks of material misstatement
- Obtaining sufficient appropriate audit evidence about the completeness and accuracy of information produced by the broker-dealer or the broker-dealer's service organization
- Performing procedures to test the relevant assertions

### Assessing and Responding to Risks of Material Misstatement Due to Fraud

- Appropriately applying professional skepticism throughout the audit
- Performing substantive procedures, including tests of details, specifically responsive to assessed fraud risks
- Identifying improper revenue recognition as a fraud risk or demonstrating how the presumption of fraud risk related to revenue recognition was overcome
- Addressing the risk of management override of controls, including testing journal entries

### Customer Protection Rule

- Testing the completeness and accuracy of significant components of the customer reserve computation and possession or control information reported in the supplemental information

## Engagement Quality Review

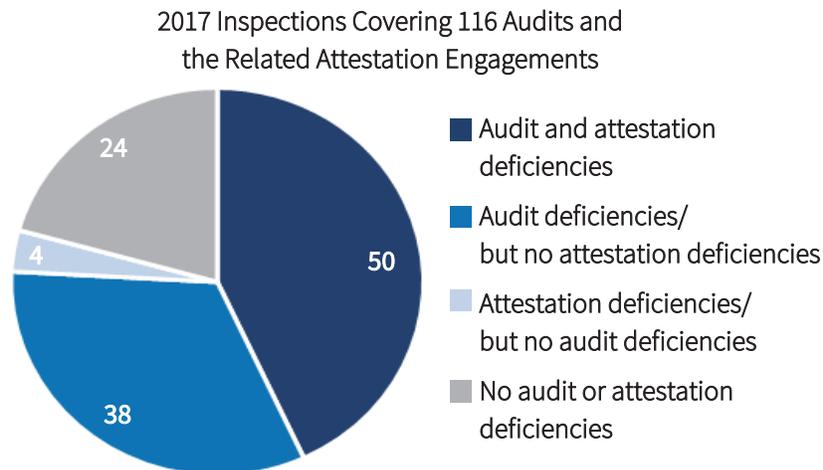
- Having an engagement quality review performed by a qualified reviewer who appropriately evaluates the assessment of, and audit responses to, identified significant risks

## Examination Procedures

- Testing controls over compliance with the financial responsibility rules during the year, and as of year-end, including testing the completeness and accuracy of information used in the controls

## 2017 Inspection Results

This is the third year of inspections since the new attestation engagements were required and PCAOB standards were required to be followed for broker-dealer audits and the related attestation engagements. A high number of deficiencies in the audits and attestation engagements of broker-dealers continued to be identified. Many of the deficiencies observed are consistent with those described in previous annual reports.



## Fewer Independence Violations

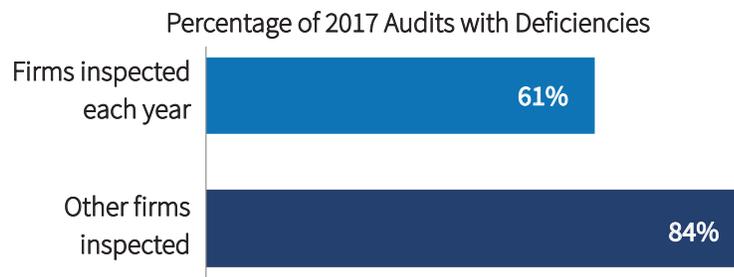
Only four independence violations were identified during 2017, or eight percent of the audits where independence was a focus area, compared to 10 percent in 2016. Further, the percentage of audits with violations observed since the inception of the interim inspection program has declined. The collective efforts of inspections, enforcement actions, and outreach through our [forums](#) and [webinars](#) appear to be helping auditors better comply in this area.

## Fewer Audits with Deficiencies at Firms that Also Audited Issuers and at Firms Inspected Each Year

Audit firms with greater experience conducting audits pursuant to PCAOB standards and that have this work regularly inspected have fewer audits with deficiencies.

Firms that also audited issuers had fewer audits with deficiencies in 2017 compared to audits performed by firms that did not audit issuers. Twenty-seven of the 28 audits with no deficiencies in 2017 were performed by firms that also audited issuers.

In addition, fewer deficiencies in 2017 were identified at firms whose broker-dealer audits were also inspected in each of the prior two years compared to the firms that were not inspected in all three years.



## Considerations for Broker-Dealer Owners and Audit Committees (or Equivalent)

Broker-dealer owners and audit committees (or equivalent) benefit from a meaningful dialogue with their auditors. Asking their auditors about how the items described in the Annual Report are being addressed in their audits and the related attestation engagements could encourage their auditors to take appropriate actions to avoid these types of deficiencies.

Examples of matters that owners and audit committees (or equivalent) of all broker-dealers are encouraged to discuss with their audit firms are as follows:

### Prior to Appointment or Retention

- How does the firm determine compliance with the independence criteria set out in the rules and standards of the PCAOB and the rules of the SEC?
- What is the firm's experience with auditing broker-dealers and performing audits in accordance with PCAOB standards? How does the firm determine that personnel assigned to the audit, including the engagement quality reviewer, have the relevant knowledge, skill, and ability to audit broker-dealers?
- Has the firm ever been inspected by the PCAOB? If so, what were the inspection findings and what corrective actions were taken?

## During the Audit

- How is the firm assessing and responding to fraud risk, including fraud risk specific to revenue recognition?
- Is the firm relying on management controls to alter the nature, timing, and extent of its substantive testing procedures? If so, what are the controls and how did the auditor assess the design and operating effectiveness of those controls?
- What financial information does the firm use in testing the customer reserve computation? What does the firm do to determine whether the information is complete and accurate?
- How does the firm determine whether the schedule for possession or control of customer securities is fairly stated in all material respects?

## At the Conclusion of the Audit

- Did the firm have the required engagement quality review performed for both the audit and attestation engagement?
- What are the qualifications of the engagement quality reviewer who performed these reviews?

## Outreach and Other Information

The PCAOB remains committed to outreach in various forms. The [forums](#) for auditors of broker-dealers include discussions related to inspection observations, standard setting, and enforcement matters. Information is also shared periodically in other ways, such as [webinars](#), that provide educational opportunities related to the audits of broker-dealers. In addition, certain relevant standards and helpful releases and guidance can be found [here](#).

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