

**RHR SMITH AND COMPANY**

**QUALITY CONTROL DOCUMENT**  
**March 1, 2011**

## **RHR Smith & Company Code of Conduct**

RHR Smith & Company complies with all professional standards of conduct, including those established by the American Institute of Certified Public Accountants (AICPA).

As a company we

1. accept the solemn responsibility of the public trust;
2. meet or exceed expectations in matters of confidentiality, honesty, integrity, and professional excellence;
3. maintain independence and objectivity;
4. observe both the form and the spirit of technical and ethical standards;
5. discharge professional responsibilities with competence and diligence;
6. properly use government information and resources;
7. respect the auditor/client relationship
8. behave professionally and treat our clients with respect at all times.

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## INTRODUCTION AND FIRM BACKGROUND

Our firm was founded in 1997 after Michael G. Hulsey and Ronald R. Smith gained several years experience with a local CPA firm. In August of 2001 Ron H.R. Smith became the sole shareholder after Michael G. Hulsey decided to pursue other things. Currently, full-time staff consists of 16 professional employees.

Our firm's objectives are to:

- provide high quality auditing, accounting, tax and management advisory services to clients in our geographic area,
- help our clients reach their maximum potential through sound and efficient accounting, financial, and management practices,
- offer outstanding customer service, distinguished by our personalized approach, timely responses, professionalism and accuracy, and
- distinguish our firm as a leader in our profession by promoting and adhering to the most demanding professional standards.

In order to achieve these objectives, our firm

- has adopted a Quality Control System described in this document ensuring the highest standards of technical competence and ethics, and
- engages with clients, an advisory board, agencies and professional associations to continuously inform processes for improvements to customer service.

Our firm will realize sustainable growth through a combination of expanded service to current clients and the careful addition of new clients.

Our firm serves clients from an office located in Buxton, Maine. We are licensed to practice in the States of Maine, New Hampshire and Vermont. Our audit clientele currently consist of governmental and nonprofit organizations.

Ronald H.R. Smith, CPA serves as the Managing Owner of the firm.

## **LEADERSHIP RESPONSIBILITIES FOR QUALITY WITHIN THE FIRM**

It is our firm's policy to promote a culture of high quality that pervades our operations through the development of, and adherence to, a system of quality control. (QC) Firm management, under the direction of the managing owner, assumes responsibility for our firm's system of quality control and designs the system to

- emphasize the importance of performing work that complies with professional standards and regulatory and legal requirements, and
- issue reports that are appropriate in the circumstances.

In maintaining a culture of high quality, our firm emphasizes the importance of ethics and integrity in every decision that personnel make, particularly at the engagement level. The firm ensures compliance with this policy by implementing the following procedures:

1. The firm dedicates sufficient and suitable resources to its quality control system, and to supporting high quality among staff. Individuals who have the operational responsibility for the quality control system have the expertise, experience and authority to identify, develop and implement the necessary QC policies and procedures. The firm appropriately communicates clear, consistent, and frequent actions and messages that emphasize the firm's QC policy and procedures. These include:
  - a. Providing a copy of the firm's QC document to all new professional employees and reviewing the importance of the document with them.
  - b. Reviewing the firm's QC policies and procedures, especially in areas where questions or problems have arisen, with personnel during training sessions.
2. The managing owner evaluates client relationships and engagements to ensure that commercial considerations were not placed ahead of the firm's commitment to quality control. Additionally, the firm's compensation and advancement policies and procedures (covered in Human Resources Section) do not place commercial considerations ahead of the quality of work performed.
3. The managing owner of the firm demonstrates the importance of high quality by their actions, such as:
  - making decisions with a focus on the public interest and emphasizing that personnel do the same,
  - demonstrating the importance of creating and maintaining a good public reputation,
  - ensuring staff have sufficient time and resources to solve engagement challenges,

- following the spirit, as well as the letter, of professional, regulatory and legal standards,
  - Displaying enthusiasm and sincerity in communicating their commitment to a quality initiative, and
  - Demonstrating consistency.
3. The firm establishes a formal code of conduct that reflects the firm's core value of high quality and guides personnel to make appropriate decisions throughout their workday. The code of conduct is regularly communicated and reiterated to all employees and is posted in various common areas throughout the office.
  4. The engagement partner assumes responsibility for the overall quality of each audit engagement to which he is assigned and sets an appropriate example to other team members throughout all stages of the engagement.
  5. The firm establishes and maintains a positive work environment by combining the firm's quality objectives with the personnel's needs to be valued and appreciated.
  6. The firm hires, compensates and promotes those who possess and exhibit high levels of integrity (see Human Resources section).
  7. The firm provides ethics training for all professional personnel at least every three years (See Relevant Ethical Requirements section).
  8. The firm rewards personnel who demonstrate a commitment to high quality through its performance evaluation, compensation and advancement system (See Human Resources section).
  9. The firm does not allow unethical behavior to go unchallenged. We address instances of noncompliance with our QC system through swift disciplinary and corrective action, or in extreme cases, termination of the offending employee.
  10. At least annually, the firm's policies and procedures are reviewed to determine if leadership responsibilities are appropriate and operating effectively (See Monitoring section).

## RELEVANT ETHICAL REQUIRMENTS

It is our policy that all professional personnel be familiar with and adhere to relevant ethical requirements of the AICPA, contained in the *Code of Professional Conduct*, the State of Maine Board of Accountancy, and the Maine CPA Society in discharging their professional responsibilities.

It is the policy of our firm that, for engagements subject to *Government Auditing Standards* and other applicable regulatory agencies, all professional personnel will be familiar with and adhere to the relevant ethical requirements in those standards, and that personnel will always act in the public interest.

It is our policy that when the firm and its professional personnel encounter situations that potentially threaten independence but are not specifically addressed by the independence rules of the AICPA *Code of Professional Conduct*, the situation will be evaluated by referring to the *Conceptual Framework for AICPA Independence Standards* and applying professional judgment to determine whether a breach of independence has occurred. The firm will take appropriate action to eliminate those threats, or mitigate them to an acceptable level by applying safeguards. If effective safeguards cannot be applied, the firm will withdraw from the engagement or take other corrective actions as to eliminate the breach.

### *Prohibited Transactions and Relationships*

Although not necessarily all inclusive, the following are considered to be prohibited transactions and relationships.

1. Borrowing from or loans to a client, or client's personnel during the period of a professional engagement by any employee of the firm.
2. Accepting or offering gifts or entertainment from or to a client unless reasonable in the circumstances and approved by the managing owner.
3. Certain family relationships between professional personnel and client personnel. Consult the managing owner for a ruling on such relationships.

Notwithstanding the preceding policy and list of prohibited transactions and relationships, at the managing owner's certain prohibitions can be waived if it is deemed to be in the best interest of the firm. However, in so doing the engagement service performed for the client must be limited to that allowed by AICPA professional standards.

The firm ensures compliance with these policies by implementing the following procedures:

1. All professional personnel are required to sign a representation letter when hired (and annually thereafter) that acknowledges their familiarity with the firm's

relevant ethical requirements policies and procedures, particularly regarding independence. Such signed representation letters are also required from part time, seasonal, and contract professionals and any other individuals who work on accounting and auditing engagements and are required to be independent. Ethics training, is provided to professional personnel at least every three years, and is provided more often if required by licensing entities in other states in which the firm conducts engagements. The training covers the firm's relevant ethical requirements policies and procedures, and the independence and ethical requirements of all applicable regulators..

2. All professional personnel review the current client list in conjunction with completing the representation letter for identifications of threats to, or breaches of independence. The current client list is maintained by the Operations Director. Additions to the firm's client list are communicated to all personnel on a timely basis by memorandum from the managing owner.
3. If a potential threat to independence is identified, the managing owner accumulates and communicates relevant information to appropriate personnel so:
  - a. the firm and the engagement manager can determine whether they satisfy independence requirements,
  - b. the engagement manager can take appropriate action to address identified threats to independence, and
  - c. the firm can maintain current independence information. For clients of whom the firm is not independent, only compilation services are performed.
4. All personnel have ready access to the relevant ethical requirements the firm is subject to. Current copies of applicable independence, integrity and objectivity requirements are maintained in the firm's library.
5. The engagement partner has the primary responsibility for determining:
  - a. Compliance with relevant ethical requirements on each new and recurring clients, including independence.
  - b. a consideration of unpaid fees,
  - c. an annual confirmation of the independence of another accountant performing work on a segment of an audit, review or attestation (including forecast and projection) engagement,
  - d. appropriate reporting on compilations in which the firm is not independent,

- e. a consideration of whether actual or threatened litigation has an effect on the firm's independence with respect to the client, and
  - f. a determination of whether all professional personnel are independent of the reporting entity, if the firm is engaged as the principal auditor to report of the basic financial statement of the financial reporting entity.
  - g. Whether the firm's relationship with entities in the governmental financial statements has an effect on independence.
  - h. Whether the firm was a party to a cooperative arrangement with a client that was material to the firm or the client.
  - i. The work programs and standard forms in the accounting and auditing manuals used by the firm include steps that ensure compliance with this procedure.
6. The engagement manager has the primary responsibility to identify all nonattest services performed for an attest service client, and for determining if the nonattest services impair their independence. Reviewing nonattest services performed for attest clients includes obtaining and documenting an understanding with the client regarding the client's responsibilities for the nonattest services performed by the firm. Where applicable, this includes determining whether nonattest services impair independence under the independence rules in *Government Auditing Standards* for ongoing, planned and future audits. Firm engagement work programs for all attest and compilation engagements include steps to ensure compliance with this procedure.
7. The managing owner is responsible for obtaining the representation letters, reviewing them for completeness, and accumulating relevant information relating to identified threats in relevant ethical requirements matters, including questions from the representation letters and those from other sources.. Documentation of the resolution of a relevant ethical requirements matter is filed in the client's work paper files.
8. The managing owner is responsible for determining actions to be taken when professional personnel violate firm independence policies and procedures. The action for each incident is determined based on its unique circumstances and may include eliminating a personal impairment, requiring additional training, drafting a reprimand letter, or even termination.
9. The managing owner is responsible for monitoring the firm's independence of attest clients at which the owner or senior personnel have been offered management positions or have accepted offers of employment. The independence, integrity, and objectivity questionnaire used by the firm and the

client acceptance checklists used by the firm in attest engagements include questions to help ensure compliance with this requirement.

10. If a breach of independence is identified, the firm promptly communicates the breach and the required corrective actions to the engagement manager, who, along with the firm, has responsibility to address the breach. The breach is also communicated to other relevant personnel in the firm, and those subject to the independence requirements who may have to take appropriate action. The engagement manager confirms to the firm when required corrective actions related to the breach and noncompliance with these policies and procedures have been taken.
11. To ensure that independence is properly addressed at the engagement level, as part of the acceptance and continuance decision, the engagement partner obtains and considers relevant information about the engagement and evaluates circumstances and relationships that could cause a potential threat to independence, if any. In addition, for audit engagements, the engagement partner forms a conclusion on compliance with independence requirements.
12. All professional personnel remain alert for any evidence of noncompliance with relevant ethical requirements during the engagement and are required to promptly notify the engagement partner of any circumstances or relationships that may create a potential threat to independence, such as a prohibited transaction or an independence breach, so that appropriate action can be taken.
13. If the firm is engaged as a principal auditor and another firm is engaged to audit a subsidiary branch, division, governmental component unit, or to perform procedures on an element or account grouping, within a client's financial statements, the engagement team does not rely on the other auditor's work.
14. The managing owner is responsible for monitoring the firm
15. At least annually, the managing owner reviews the firm's ethical requirements policy and procedures to determine if they are appropriate and operating effectively (See Monitoring section).

## **ACCEPTANCE AND CONTINUANCE OF CLIENTS AND ENGAGEMENTS**

It is our firm's policy that, for all compilation, review, audit and attestation engagements, the acceptability of the client and the engagement be evaluated before the firm agrees to provide professional services. The firm will accept engagements only after it has considered the integrity of the client, and believes the engagement can be completed with professional competence after considering the risks associated with providing professional services in the particular circumstances. The firm ensures compliance with this policy by implementing the following procedures:

1. For each prospective client (or existing tax or consulting client) that requests for the first time a compilation, review, audit, or attestation service, the managing owner is required to complete or approve an engagement acceptance form.
2. For existing clients, the managing owner and senior staff members annually reviews the firm's client list and reevaluates the acceptability of each client and engagement. Reasons the firm or managing owner may consider discontinuing services include significant changes in the client and its operations, or conditions that would have caused the firm to reject the client if they had existed when the client was originally accepted. Furthermore, the engagement work programs used by the firm contain steps requiring the engagement team to consider whether the firm should discontinue providing all or certain services to a client. (See Engagement Performance section).
3. The managing owner documents how issues identified during the acceptance and continuance process were overcome and resolved, allowing the firm to accept or continue the client relationship or specific engagement. This documentation includes discussion of significant issues, consultations, conclusions, and the basis for the conclusions.
4. The managing owner is notified of any instances in which the firm should discontinue providing all or certain services to a client or should withdraw from a specific engagement. The managing owner should consider whether outside legal counsel should be consulted in making that decision. The engagement team will be notified by the managing owner of the name of any client to which services are discontinued. Significant issues, consultations, conclusions, and the basis for conclusions should be documented when withdrawal from an engagement and/or client relationship occurs.
5. The managing owner is responsible for ensuring that an engagement letter is obtained for each client. The engagement letter should document the firm's understanding with the client regarding the nature, scope, and limitations of services to be performed. Supervisory staff and his or her role are defined as part of the staffing plan for each client.
6. For audit engagements, the engagement partner is responsible for

- a. Becoming satisfied that the appropriate procedures regarding the acceptance and continuance of client relationships and specific audit engagement have been followed.
  - b. Determining that the acceptance and continuance conclusions reached are appropriate
  - c. When information is obtained that would have caused the firm to decline the engagement, had such information been known initially, promptly communicating such information to the firm so that the firm and the engagement partner can take necessary action.
7. If the firm discovers a potential conflict of interest during the acceptance and continuance decision, the managing owner determines whether it is appropriate to accept or continue the engagement. If the engagement is accepted, the ethical requirements under AICPA Interpretation No. 102-2 “Conflicts of Interest,” under Rule 102. *Integrity and Objectivity* are considered.
8. At least annually, the managing owner reviews the firm’s acceptance and continuance of client relationships and specific engagement policy and procedures to determine if they are appropriate and operating effectively (See Monitoring section).

## HUMAN RESOURCES

The success of our firm depends on its professional staff. Our firm intends to succeed in the marketplace by having staff that possess the capabilities, competence and commitment to ethical principles to ensure that engagements performed by the firm are in accordance with professional standards and regulatory and legal requirements and that appropriate reports are issued. Having effective QC policies and procedures over human resources will help ensure the proficiency of our personnel.

Our comprehensive human services Quality Control System includes policies and procedures for:

- Recruitment and hiring,
- Determining capabilities and competencies,
- Assignment of personnel to engagements,
- Professional development, and
- Performance evaluation, compensation and advancement.

It is our firm's policy that recruitment and hiring decisions be based on an objective evaluation of the firm's personnel needs, that candidates possess the appropriate characteristics to perform competently, and that new employees are adequately informed of the firm's policies and procedures. The firm ensures compliance with its policy by implementing the following procedures.

### 1. Recruitment and Hiring

- The managing owner annually plans the firm's long-range personnel objectives. Current clientele, anticipate growth, personnel turnover, individual advancement and retirement are among the criteria considered. The plan is communicated with those involved in the hiring process.
- The managing owner makes the recruitment decisions with strong input from the Operations Director, respective Division Directors and Human Resources Director.
- The Operations Director and Human Resources Director screen all applicants before hiring. After approval, the managing owner makes a final decision.
- New employees are informed by the human resources director about the firm's policies and procedures on or before their first day of employment. A copy of this quality control document is also presented to newly hired personnel.

### 2. Determining Capabilities and Competencies

It is our firm's policy to determine whether individual members of the professional staff possess necessary capabilities and competencies. In making this determination, the firm primarily considers qualitative measures, as opposed to quantitative ones. The firm ensures compliance with this policy by implementing the following procedures:

- Periodically, the managing owner and Operations Director assess the competencies that individuals who are responsible for supervising attest engagements and signing attest engagement reports should possess. This assessment includes:
  - an understanding of the firm's system of quality control and the *Code of Professional Conduct*,
  - an understanding of the performance, supervision, and reporting standards at the level of service to be provided,
  - an understanding of the applicable accounting, auditing, and attestation professional standards, including those directly related to any special industries,
  - an understanding of the applicable industries and each industry's organization and operating characteristics sufficient to identify high or unusual risk areas and to evaluate the reasonableness of industry-specific estimates,
  - proficiency and seasoned judgment in discharging assigned responsibilities, and
  - when applicable, an understanding of how an organization is dependent on or enabled by information technologies and how the information technology systems are used to record and maintain financial information.
- The firm considers other capabilities and competencies as needed in the circumstances, which may include:
  - Various personal attributes, such as integrity and ethics, professionalism, project management skills, etc,
  - Leadership qualities, including strategic thinking and planning, negotiating and persuading, teamwork, problem solving, coaching and empowerment, etc, and
  - Perspective on business issues, such as managing and developing people, marketing and selling, knowledge of best practices, business advisory skills, etc.
- The firm determines how personnel can best obtain additionally needed capabilities and competencies.
- Performance evaluations are conducted at least annually to determine competencies and capabilities possessed by personnel.

### 3. Assignment of Engagement Teams

It is our firm's policy that each engagement be supervised by a lead auditor (engagement manager) with appropriate authority. Additionally, staff assigned to engagements possess the necessary capabilities, competencies and available time to

- a. Perform engagements that comply with professional standards, regulatory and legal requirements, and
- b. Enable the firm to issue reports that are appropriate in the circumstances. The firm ensures compliance with this policy by implementing the following procedures:
  - In addition to assessing the engagement team's capabilities and competencies (See Determining Capabilities and Competencies Section), the managing owner or Division Director clearly defines and communicates the responsibilities and authority of a lead auditor to that individual, and evaluates the lead auditor's work load to ensure the individual has time to adequately perform the role.
  - The identity and role of the lead auditor is communicated to client management and those charged with governance through a client Staffing Plan.
  - Periodically the managing owner prepares (or directs the preparation of) a Staffing Plan, which is circulated to all employees.
  - The firm recognizes that many modifications to the Staffing Plan will be required because of changes in client circumstances that affect the competencies appropriate for that client engagement, based on an informal meeting of the owner and managers affected by the changes, and after a reconsideration of the planning factors described above. Any disputes regarding assignment of personnel are resolved by the Operations Director. Any appeals to that resolution should be made to the managing owner.
  - Changes in the Staffing Plan are communicated verbally to the appropriate staff person by the managing owner or Operations Director.

#### 4. Professional Development

It is our firm's policy that all professional personnel complete continuing professional education necessary to ensure compliance with Maine Board of Accountancy licensing, American Institute of Certified Public Accountants Government Audit Quality Center, Government Auditing Standards, and US Government Accountability Office and other regulatory agencies if applicable. The procedures below are followed to ensure compliance with this policy:

1. A Firm CPE Planning Worksheet is prepared annually and is approved by the managing owner. The managing owner and Operations Director monitors the progress of employees in achieving this plan.

2. All professional personnel must obtain a minimum of 40 hours of CPE each year in programs that qualify for credit under the CPE rules that govern the firm.
3. In each two year reporting period, individuals responsible for planning, directing, conducting substantial portions of fieldwork, or reporting on audits under the *Government Auditing Standards* must obtain 24 hours of CPE in subjects directly related to the government environment and governmental auditing, or the specific or unique environment in which the audited entity operates. In addition, auditors who do any amount of planning, directing, or reporting on Yellow Book assignments and auditors who are not involved in those activities but charge at least 20% annually of their time to Yellow Book assignments are required to also obtain at least another 56 hours (for a total of 80 hours) of CPE that enhances their professional proficiency to perform audits or attestation engagements. In other words, everyone working on a Yellow Book engagement has to meet the 14 hour requirement. However, auditors who do not do any planning, directing or reporting on a Yellow Book engagement or who do not spend at least 20% of their time annually on Yellow Book engagements are not required to obtain an additional 56 hours of CPE to comply with the 80-hour requirement.

In accordance with the membership requirements of the AICPA Government Audit Quality Center's membership requirements, the Quality Control Manager must meet both the 24 hour and 80 hour CPE requirements even if that individual would not otherwise be subject to those requirements. The QC Manager must also participate in the annual Center sponsored webcast on recent developments in governmental auditing.

4. Appropriate CPE records are maintained for each professional for five years.
  5. Information about current developments in professional standards and/ or literature, and materials containing the firm's policies and procedures are made available to personnel.
  6. The firm recognizes that on-the-job training accounts for a significant part of professional development and encourages personnel with supervisory responsibilities to be aware of situations where it can be provided.
  7. The firm recognizes the benefits of other professional development activities and encourages personnel at each staff level to participate in these activities
5. Performance evaluation, compensation and advancement

It is the policy of the firm to evaluate performance, compensation and advancement continuously and advise personnel of their progress periodically. The professional selected for advancement should have the necessary qualifications to fulfill their assigned responsibilities and compensation of personnel is based on the quality of their work. The following procedures are followed to ensure compliance with this policy:

- The following personnel levels and performance requirements are used by the firm:
  - a. **Managing Owner** – Responsible for the overall success of this firm.
  - b. **Operations Director** – Assists Managing Owner/Partner with overall operations of the firm
  - c. **Division Directors**—Assumes responsibility for each functional service division in the firm
  - d. **Audit Manager**—Assumes responsibility of day-to-day direction of the client engagement and proper performance of field work.
  - e. **Staff Accountant**—Assumes responsibility of unaudited financial statements, segments of audits under the supervision or more experienced staff.
  - f. **Human Resources Director** Assumes responsibility to maintain all areas of employment records.
  - g. **Accounting Specialist**—Assumes responsibility as an accountant with support to all levels of accounting staff.
  - h. **Development Staff Consultants** – Performs consulting services unrelated to audit and accounting.
  - i. **Quality Control Manager** – Responsible for implementing, updating and conducting training related to Quality Control Policies and Procedures.
  - j. **Intern** – Has a basic understanding of accounting and bookkeeping, but may not have obtained a college degree that includes a significant concentration of accounting courses.
- All professional staff is evaluated by their supervisors annually and receives a counseling interview conducted by the managing owner, Operations Director and/or the respective Division Director. As part of this evaluation, each staff member completes a self evaluation.
- The managing owner makes advancement and termination decisions with input from the Operations Director and Human Resources Director.

## **ENGAGEMENT PERFORMANCE**

Engagement performance encompasses many aspects of performing an engagement, from the initial planning stages to the issuance of the report and assembly of the workpapers. It is not uncommon for our firm's engagement teams to occasionally encounter complex or contentious issues that result in the need for consultation or that create differences of opinion. Our firm believes in a strong QC system and supports frequent engagement QC review. While all of these activities are part of the engagement performance element of the QC system, our firm has differentiated certain activities included in this document for ease of understanding. The activities are segregated as follows:

- Engagement performance and documentation
- Engagement quality control review
- Consultation and differences of opinion

Policies and procedures for each of these activities are described below. At least annually, the managing owner reviews the firm's engagement performance policies and procedures to determine if they are appropriate and operating effectively. (See Monitoring Section).

### 1. Engagement Performance and Documentation

It is our firm's policy that all compilation, review, audit, and attestation (including forecasting and projection) engagements can be properly planned, performed, supervised, reviewed, documented, and reported or communicated according to professional standards, regulatory, legal requirements, of the firm. In this regard, the firm's system of engagement performance QC steps is documented in the firm's engagement performance bridging documents. It's the responsibility of the engagement partner and the engagement team for implementing the firms' QC steps indicated on the bridging documents.

The firm adopts and integrates within its quality control system the use of PPC and other accounting and auditing manuals and practice aids as more fully described in the engagement performance bridging documents, attached as an appendix to this document. Nothing within this QC document should be construed as requiring a higher level of performance or documentation than the minimum specifically required by our firm's QC policies and procedures, nor to override the exercise of professional judgment.

The firm ensures the protection of the confidentiality, custody, integrity, accessibility and retrievability of engagement documentation through staff training and personnel policies and procedures..

### 2. Engagement Quality Control Review

It is our firm's policy to evaluate all engagements against criteria established by the firm to determine whether an engagement quality control review should be performed, and to perform an engagement quality control review for all engagements that meet those criteria. Engagement QC reviews are completed before the report is released. The firm ensures compliance with this policy by implementing the following procedures:

- a. The firm establishes criteria for performance of an engagement quality control review (EQCR). In establishing such criteria the firm considers:
  - i. the structure and nature of the firm's practice,
  - ii. the nature of the engagement, including whether it involves a matter of public interest,
  - iii. whether unusual circumstances or risks have been identified relating to the engagement, engagement service type or industry, and
  - iv. whether laws or regulations require an EQCR to be performed.
- b. The firm establishes a different set of criteria for each major type of service provided. All engagements are evaluated against the criteria. An EQCR is performed for all engagements that meet established criteria. If no engagements meet the criteria established by the firm for EQCR, no reviews are performed.
- c. The firm may periodically make changes to the established criteria based on changes in the firm's practice.
- d. Based on the current composition of the firm's accounting and auditing engagements, the firm has concluded that EQCR should be performed for all audit engagements. Reviews and compilations are not required to have EQCR performed.
- e. Performing an EQCR includes the following procedures:
  - i. an objective evaluation of significant judgments made and the conclusions reached in formulating the report,
  - ii. reviewing the resolution and conclusions reached regarding differences of opinion and matters requiring consultation for appropriateness,
  - iii. considering the evaluation of the firm's and the engagement team's independence in relation to the specific engagement,
  - iv. reading the financial statement or other subject matter information and the report and considering whether the report is appropriate,
  - v. a review of selected engagement documentation relating to the significant judgments and the conclusions reached,
  - vi. a discussion with the engagement manager about significant findings and issues,

- vii. the EQCR may be conducted at various stages throughout the engagement to ensure that significant issues may be resolved to the reviewer's satisfaction before the report is released, and
  - viii. the extent of the EQCR may depend upon, among other things, the complexity of the engagement and the risk that the report might not be appropriate for the circumstances.
- f. If differences of opinion occur between the engagement manager and the EQCR, appropriate differences of opinion procedures are followed (See Consultation and Differences of Opinion section) and documentation of the resolution of conflicting opinions is finalized before the release of the report.
- g. The firm prepares appropriate documentation of the EQCR, including documentation that reflects:
  - i. The EQCR procedures required by firm policies have been performed,
  - ii. The EQCR was completed before the report was released, and
  - iii. The reviewer was not aware of any unresolved matters that would have caused him or her to believe that significant judgments made and conclusions reached were not appropriate.
- h. The firm addresses the appointment of EQCR reviewers and the technical qualifications required to perform this role, including the necessary authority and experience. In selecting appropriate EQC reviewers, the following criteria are followed:
  - i. the EQC reviewer is selected by the managing owner,
  - ii. the EQC reviewer has sufficient and appropriate experience, technical expertise, and authority for the engagement to be reviewed,
  - iii. the EQC reviewers maintain appropriate ethical requirements, such as objectivity, due professional care, and independence. The EQC reviewer satisfies the independence requirement relating to the engagement reviewed, and
  - iv. the EQC reviewer does not participate in the performance of the engagement except in a consulting role, if for example, there is a question regarding whether a judgment made by the engagement manager is acceptable to the EQC reviewer. Both the EQC reviewer and the engagement team are careful to maintain the reviewer's objectivity.
- i. When the firm does not have qualified personnel to perform the EQCR, the firm contracts with qualified external individuals or other firms to

perform the review. The criteria in Procedure 3 are followed in selecting qualified external EQC reviewers.

### 3. Consultation and Differences of Opinion

It is our firm's policy that personnel refer to authoritative literature or other sources when appropriate. It is our firm's policy that all professional personnel seek timely consultation whenever differences of opinion occur or uncertainty exists about the answer to a technical question. The firm ensures compliance with this policy by implementing the following procedures:

- a. The firm maintains or provides ready access to an adequate and up to date reference library that includes materials related to clients served and that should be consulted to assist professional staff in their research of technical issues.
- b. While it is impossible to list all situations that might require referral to authoritative literature or other sources, or that might require consultation, the following complex situations may require consultation:
  - i. any engagement in which a qualified or nonstandard report is likely to be issued,
  - ii. any engagement involving material litigation,
  - iii. application, for the first time, of new or complex technical pronouncements,
  - iv. industries with special accounting, auditing, or reporting requirements,
  - v. accounting for complex or unusual transactions,
  - vi. emerging practice problems,
  - vii. choices among alternative generally accepted accounting principles upon initial adoption or when an accounting change is made,
  - viii. reissuance of a report, consideration of omitted procedures after a report has been issued, or subsequent discovery of fact that existed at the time a report was issued,
  - ix. filing requirements of regulatory agencies, and
  - x. meetings with regulators at which the firm is to be called on to support the application of generally accepted accounting principles or generally accepted auditing standards that have been questioned.
- c. Issues regarding consultation are first discussed by members of the engagement team. If further consultation is necessary, individuals within the firm having appropriate expertise are then consulted.
- a. Consultations with specialists outside the firm, including nonaccounting specialists, must be approved by the engagement manager and managing owner.

- b. All known relevant facts are provided to those consulted so they can understand the nature and scope of the consultation.
- c. All consultation involving unusual, contentious, unfamiliar, or difficult issues should be adequately documented to facilitate understanding of the issue for which consultation was needed, the results of the consultation, the decisions made and their basis, and how those decisions were implemented.
- d. If a difference of opinion occurs within the engagement team, between the engagement manager and the EQC reviewer, or with those consulted within or outside the firm, the difference will be resolved using Procedures c & d above, if possible. If not, the matter should be brought to the attention of the managing owner. The managing owner, with assistance from other practitioners or regulatory agencies if desired, will resolve the dispute in question. The conclusion reached and how that conclusion will be implemented should be documented. In addition, any party to the consultation/difference of opinion who disagrees with the final conclusion may document his or her disassociation from the final resolution. The firm will not release the report until any differences of opinion are resolved.
- e. For audit engagements, the engagement partner is responsible for ensuring that appropriate consultation is undertaken on difficult or contentious matters. Additionally, the engagement partner ensures that
  - i. Members of the engagement team follow the firms consultation policies during the course of the engagement.
  - ii. The nature and scope of the consultation are agreed upon with the party consulted
  - iii. The resulting conclusions are understood by the party consulted
  - iv. Such conclusions are implemented.

## MONITORING

It is the firm's policy that our quality control system be monitored on an ongoing basis to provide the firm with reasonable assurance that the policies and procedures established by the firm for each of the other elements of quality control are suitably designed and are being effectively applied. The adequacy, relevance and effectiveness of the firm's QC system are monitored on an ongoing basis by the managing owner and quality control manager. Monitoring activities include engagement quality control review (EQCR), inspection and post issuance review. EQCR, performed prior to completion of the engagements, assists in providing ongoing consideration and evaluation of the firm's QC system. The policy and procedures relating to EQCR are discussed elsewhere in this document. (See Engagement Performance section). The retrospective monitoring activities performed by the firm relate to inspection and post issuance review (inspection/review) and are the primary activities addressed in these monitoring policies and procedures.

As an integral part of the monitoring process, our quality control system is inspected annually to determine whether the firm has complied with applicable professional standards and its stated quality control policies and procedures. The procedures listed below are followed to ensure compliance with this policy:

1. Bi-annually the firm's compliance with its quality control system is reviewed by an individual or team (inspector) appointed by the managing owner. The inspection is planned, performed, and documented using the appropriate monitoring program in Chapter 12 of *PPC's Guide to Quality Control* as a work program. The monitoring procedures include review of administrative records to assess compliance relating to QC elements other than engagement performance. The monitoring process will include a review of the governmental audit practice and each type of plan in the firm's ERISA employee benefit plan audit practice in accordance with the membership requirements of the respective audit quality centers.
2. At the conclusion of the inspection, the inspector is responsible for (a) discussing the results of the review with the supervisory personnel responsible for each of the selected engagements and (b) summarizing the deficiencies for each engagement reviewed and (c) determining whether any corrective action needs to be taken or improvements made with respect to those specific engagements. Once identified, the deficiencies are summarized and evaluated to determine whether:
  - a. existing quality control policies and procedures should be modified,
  - b. additional emphasis should be placed on specific industries or areas for future engagements,

- c. appropriate competencies are being achieved for accounting, auditing and attestation engagements, and
  - d. the scope of the inspection, the findings, and the recommendations are then reported to the managing owner. The findings for the engagements selected for review are also discussed with the professional staff.
- 3. The firm pursues one or more of the following actions resulting from its evaluation of the deficiencies noted during inspection:
  - a. take remedial action directed toward the individual engagement or person,
  - b. revise the firm's QC policies and procedures,
  - c. discipline individuals who fail to follow the firm's QC policies and procedures, and
  - d. communicate the findings to those responsible for training and professional development.
- 4. If the monitoring results reveal that an issued report is inappropriate or that procedures were omitted during the performance of the engagement, the firm determines what further actions are required to comply with relevant professional standards and applicable laws and regulations.
- 5. At least annually, the firm prepares and distributes a formal inspection/review report to all professional personnel. This annual monitoring communication provides a description of
  - a. monitoring procedures performed,
  - b. the conclusions reached from such procedures, and
  - c. any systemic, repetitive, or other significant deficiencies noted and corrective actions taken to resolve them.
- 6. In addition, the firm is subject every three years to a peer review in accordance with the requirements of the AICPA. The managing owner is responsible for scheduling and coordinating that review. The findings for the engagements selected for review during the peer review are discussed with the professional staff.
  - a. In accordance with the membership requirements of the AICPA Governmental Audit Quality Center, the engagement letter covering the firm's peer review will require that the governmental audits selected for review during the firm's peer review be reviewed by someone who is an employed member firm of the respective Center. Also, information relative to the firm's most recently accepted peer review is available to the public in accordance with the membership requirements of the respective Centers.
  - b. The internal inspection results are made available to the firm's peer review team.

7. Based on the firm's annual inspection and, if appropriate, the results of the firm's peer review, the managing owner determines any corrective actions that should be pursued to improve, amend, or rectify the QC system.
8. The firm management and owner meet at least annually and discuss the monitoring process, the results of the inspection/review, the corrective actions determined to be needed by the managing owner and consider the implications for the firm.
9. The managing owner is responsible for monitoring and documenting the implementation of and compliance with any corrective actions.
10. The managing owner periodically reminds personnel during staff meetings that any concerns regarding complaints or allegations may be communicated to the firm without fear of reprisals. The firm appropriately addresses complaints and allegations by:
  - a. establishing channels of communication for complaints and allegations through communicating such information to employees and clients,
  - b. investigating complaints and allegations and involving legal counsel if considered necessary. The firm assigns individuals to this process who are trained and knowledgeable about firm procedures and who are not otherwise involved in the engagement relating to the complaint or allegation, and
  - c. documenting all complaints and allegations.
11. The firm documents the performance of each element of its QC system on an ongoing basis, in conjunction with documenting its monitoring of the system. Documentation includes:
  - a. evidence of the monitoring procedures performed, including how engagements were selected for review,
  - b. evaluation of the firm's adherence to professional standards and regulatory and legal requirements,
  - c. evaluation of whether the QC system is appropriately designed and effectively implemented,
  - d. evaluation of whether QC policies and procedures are operating effectively so reports issued are appropriate for the circumstances, and
  - e. identification of deficiencies noted, an evaluation of their effect on the QC system, and the basis for determining what further actions are necessary, if any.
12. The firm retains monitoring documentation for a time sufficient to allow those monitoring the QC system, including peer reviewers to evaluate the firm's compliance with its system. The firm generally retains such documentation until the next peer review report has been completed.