

## Quality Control (ISQC 1)<sup>1</sup>—Recommendations on the Proposed Way Forward for Engagement Quality Control Reviews

### Objective of the IAASB Discussion

The objective of this Agenda Item is to discuss the Quality Control Other Working Group's (QCOWG) proposals in respect of:

- Setting the objective of an engagement quality control (EQC) review;
- Revising the definition of an EQC review;
- Determining the scope of the engagements subject to an EQC review; and
- The execution of an EQC review.

The input from the Board on these matters will assist the QCOWG in further progressing the enhancements to the requirements of ISQC 1 in relation to EQC reviews.

### Introduction

1. At the September 2016 IAASB meeting, the Quality Control Working Group presented their initial recommendations in relation to EQC reviews, in response to the feedback from respondents on the IAASB's Invitation to Comment (ITC), *Enhancing Audit Quality in the Public Interest: A Focus on Professional Skepticism, Quality Control and Group Audits*. The Board provided the QCOWG with further direction on the discrete topics presented, and accordingly this paper incorporates the QCOWG's proposals in response to the Board's feedback in relation to setting an objective, determining the scope of engagements subject to an EQC review and the execution of that review. The QCOWG is still exploring possible ways to address the topic of the eligibility of the EQC reviewer and continuing to liaise with the International Ethics Standards Board for Accountants (IESBA), therefore this issue has not been included in this paper and will be presented to the IAASB in the first quarter of 2017.

### Objective and Definition of EQC Review

#### *Board Discussion*

2. At its September meeting, the Board supported pursuing the development of an objective for EQC reviews and suggested that any proposed objective needs to reflect the fact that an EQC review is a *firm level* control that operates at the *engagement level*. The Board recommended that the EQC review remain focused on significant judgments, although was of the view that clarity was needed on what this means. Furthermore, the Board suggested that the timely performance of the EQC review be incorporated into the objective.

#### *Working Group Discussions and Recommendations*

3. In developing its recommendations, the QCOWG considered a number of sources that discuss the objective of a firms' system to manage quality, including controls to manage quality at the engagement level. In particular, the references discussed below were considered.

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<sup>1</sup> International Standard on Quality Control (ISQC) 1, *Quality Control for Firms that Perform Audits and Reviews of Financial Statements, and Other Assurance Engagements and Related Services Engagements*

4. Regulation (EU) No 537/2014 of the European Parliament and of the Council<sup>2</sup> (the EU Regulation), Article 8(1) requires that an EQC review "shall be performed to assess whether the statutory auditor or the key audit partner could reasonably have come to the opinion and conclusions expressed in the draft of these reports."

5. Further, the Public Company Accounting Oversight Board's (PCAOB) standard on Engagement Quality Control Reviews, Auditing Standard No. 7 (AS 7), includes an objective as follows:

The objective of the engagement quality reviewer is to perform an evaluation of the significant judgments made by the engagement team and the related conclusions reached in forming the overall conclusion on the engagement and in preparing the engagement report, if a report is to be issued, in order to determine whether to provide concurring approval of issuance.

6. The QCOWG also considered the current definition of an EQC review in ISQC 1 (refer paragraph 13 below), as well as its relationship to audit risk.<sup>3</sup> The QCOWG determined that while an objective needs to be established, it is necessary to amend the definition of an EQC review to establish an appropriate linkage between the definition and the objective. The QCOWG is of the view that:

- The objective should explain what the EQC review should achieve, including the mitigation of the risk of issuing an inappropriate auditor's report; and
- The definition should focus on explaining what an EQC review is.

The QCOWG also recognizes the need to reflect the concepts of quality management into the proposed objective and the proposed amendments to the definition of an EQC review.

7. In developing the objective, the QCOWG considered the reasons for extending the requirement for an EQC review beyond audits of listed entities. The QCOWG noted that an EQC review should be a control that mitigates the potential for an inappropriate conclusion on engagements that have the highest risk of material misstatement. The QCOWG was of the view that it is important to capture this consideration in the objective of an EQC review and debated if, for audits of financial statements, it was appropriate to include the term "audit failure" in the objective. However, the QCOWG agreed that this would not be appropriate terminology for the objective and the term audit failure is unique to audit engagements, yet the objective of an EQC review encompasses all types of engagements.

8. The QCOWG considered the concept of an audit failure, in particular in situations where the impact of an audit failure would be the greatest, i.e., where the entity subject to the audit failure has a large number of stakeholders or a wide range of stakeholders. Accordingly, the QCOWG considered whether it would be appropriate to include the concept of "a large number or a wide range of stakeholders" in the objective. Mixed views were expressed by the QCOWG with some members noting that particular reference to significant consequences to a large number or a wide range of stakeholders may be interpreted by some as inferring that an EQC review need not be performed on engagements that don't meet this criteria, even in situations where an EQC review may be an appropriate response by the firm. However, on balance the QCOWG determined it appropriate to include this phrase in the proposed objective and to seek the Board's view on its inclusion.

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<sup>2</sup> <http://eur-lex.europa.eu/legal-content/EN/TXT/PDF/?uri=CELEX:32014R0537&from=EN>

<sup>3</sup> The risk that the auditor expresses an inappropriate audit opinion when the financial statements are materially misstated. Audit risk is a function of the risks of material misstatement and detection risk.

9. As discussed in more detail in the “Execution of an EQC Review” section below, the QCOWG concluded that it is appropriate for the EQC reviewer to focus on the significant judgments made by the engagement team and that the timeliness of the EQC review should be emphasized, rather than its completion on or before the date of the engagement report. As a result, the QCOWG were of the view that it would be important to incorporate these aspects in the objective.
10. Based on the above considerations, the QCOWG proposes the following objective for EQC reviews:

The objective of the engagement quality control review is to provide an objective evaluation in a timely manner at appropriate stages during the engagement, of the significant judgments made by the engagement team and the conclusions reached thereon. The engagement quality control review is performed in order to respond to the risk of issuing an inappropriate engagement report, particularly in circumstances when such an issuance could have significant consequences for a large number or a wide range of stakeholders.

11. The QCOWG also considered the appropriate location for the objective in the revised standards, noting that this would be better determined once the structure of ISQC1 has been agreed and further consideration has been given as to whether a separate EQC review standard may be appropriate.
12. Based on the proposed objective, the QCOWG considered amendments to the definition that would be necessary to align the definition to the objective. The QCOWG is of the view that in order to explain what an EQC review is, the proposed definition should explain the level in a firm at which the control is set and at which it operates in order to establish accountability for the control, and the scope of the engagements that may be subject to an EQC review.
13. The QCOWG therefore proposes the following revisions to the definition of an EQC review:

As part of its overall quality management, an engagement quality control review is a response by a firm to quality risk, that operates at an engagement level, and is a process designed to provide an objective evaluation, on or before the date of the report, of the significant judgments the engagement team made and the conclusions it reached in formulating the report. The engagement quality control review process is required for audits of financial statements of listed entities, engagements for which an engagement quality control review is required by law or regulation and those other engagements, if any, for which the firm has determined an engagement quality control review is required an appropriate response to quality risk.

#### **Matters for IAASB Consideration**

1. The IAASB is asked for its views on:
  - (a) The proposed objective of the engagement quality control review, in particular the appropriateness of the phrase "significant consequences for a large number or a wide range of stakeholders"; and
  - (b) The proposed changes to the definition of an engagement quality control review.

## Scope of Engagements Subject to EQC Review

### *Board Discussion*

14. Overall, the Board supported the expansion of EQC reviews to entities other than listed entities and recommended exploring a risk-based approach. The Board emphasized the importance of the risk-based approach, and in particular, with regard to audits, addressing the public interest impact should there be an audit failure. The Board suggested that the QCOWG consider the following additional factors in its deliberations on the scope of EQC review:
- The industry in which the client operates, for example, whether it is new to the firm, or the firm does not perform many engagements in that particular sector.
  - Significant changes in the applicable framework, for example, accounting for revenue recognition or credit losses.
  - Change of key engagement personnel, or long association of key engagement personnel, with a client.
  - Current practices in local jurisdictions.
  - The likelihood, magnitude and impact of an audit failure, this is, where an audit failure would have a significant impact to the public.

### *Working Group Discussions and Recommendations*

15. In addition to the suggestions in the paragraph above, the QCOWG further considered other proposals from the Board at its September meeting, however concluded that the potential disadvantages to each of these approaches outweighed the potential benefits. These included:
- *The extension of EQC review to audits of public interest entities (PIEs).* The QCOWG determined that extending the requirement to encompass audits of PIEs would result in a more prescriptive standard that is contrary to the proposed quality management approach. Further, even if an international definition of PIE could be developed, there could be unintended consequences of mandating an EQC review for such engagements. The QCOWG noted that respondents to the ITC were also generally not supportive of this approach.
  - *Adopting an approach similar to ISA 701<sup>4</sup>* (i.e., where the standard applies to audits of listed entities and those required by law or regulation to communicate key audit matters, with the firm determining on a voluntary basis whether to communicate key audit matters in respect of other entities). The QCOWG was of the view that this approach would not result in more robust selection criteria for engagements subject to EQC review, given that extant ISQC 1 currently requires firms to determine criteria by which an engagement would be required to have an EQC review.
  - *Adopting a systematic approach to EQC reviews whereby all audits that relate to a specific industry, such as banking or insurance, are subject to an EQC review, irrespective of the assessed risk profile.* The QCOWG considered the advantages and disadvantages of such as an approach noting that the greatest advantage would be that this would ensure that certain engagements would always be subject to an EQC review. The QCOWG noted the disadvantages of this approach including:

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<sup>4</sup> ISA 701, *Communicating Key Audit Matters in the Independent Auditor's Report*

- It may be too onerous for firms, especially smaller practices, to implement.
- Not all audits in a specific industry type have the risk profile such that an EQC review would be additive to the quality of the audit.
- There is not a common definition of what constitutes a bank or an insurance company. Furthermore, it could inadvertently exclude other entities who perform a similar function but are not defined as a bank or insurance company.
- An EQC review on an engagement with a low risk profile could increase the cost of the engagement to the entity without an associated tangible benefit to the stakeholder.

The QCOWG therefore focused on how to update ISQC 1 to incorporate risk-based EQC review requirements that would provide a structure for firms to consistently set appropriately robust criteria to determine which engagement should be subject to an EQC review.

16. The QCOWG performed outreach to a number of accounting firms to better understand how the criteria for selecting engagements subject to EQC reviews is interpreted and applied in practice. The responses received by the firms in this area largely applied to audits, but some also encompassed other types of engagements. Accordingly, the following discussion will use the term "engagement" to reflect this variation.
17. Based on this outreach, the QCOWG identified that firms currently adopt a risk-based approach to determining which engagements are subject to an EQC review. Using such an approach, some firms categorize engagements and require an EQC review for those in certain of those categories. Examples of the additional criteria used by firms include engagements:
  - Where the engagement partner is a newly promoted partner or it is the engagement partner's first year on the engagement.
  - That have reports with a wide distribution.
  - Where the company is in the process of or is expected to go public in the near future.
  - That are subject to regulatory access and review, such as audits of insured or regulated depository institutions.
  - Where certain risk considerations have been identified, such as doubts over the entity's ability to continue as a going concern, higher risks identified in the acceptance and continuance process, material subsidiary or equity investee when the parent is audited by another network.
  - Where the client is a certain type of state owned or government entity.
18. The QCOWG considered why an EQC review is an appropriate control for certain engagements, in particular focusing on the current requirement in ISQC 1 that applies to audits of financial statements of listed entities. The QCOWG noted that there were certain characteristics inherent in audits of listed entities that give rise to engagement-specific risks, for example, these characteristics could include the nature of the business, the size of the entity, the number of employees or the number and range of stakeholders. The QCOWG is of the view that these characteristics could be incorporated into the risk-based criteria that a firm considers when determining which audits will be subject to an EQC review.
19. In addition, the QCOWG determined that there could be other factors that would impact the risks to quality at the engagement level for which an EQC review would be an appropriate control. Accordingly, the QCOWG suggests that the requirement includes an additional

- consideration for firms, i.e., where a risk to quality exists at the engagement level. This requirement would be supported by application material indicating the types of factors that would indicate such a risk, including the complexity of the engagement, the composition of the engagement team and the underlying reason for the performance of the engagement.
20. The QCOWG further considered whether it would be appropriate to create a separate requirement providing criteria for engagements other than audits, for which a firm would require that an EQC review be performed. However, the QCOWG noted, as it developed criteria, a considerable overlap between the criteria that could apply to an audit and the criteria that could apply to other types of engagements. As such, the QCOWG determined that one overarching requirement, covering all types of engagements and providing for separate consideration of entity specific risk factors and engagement specific risk factors, would be appropriate. Application material could then explain the application of this requirement in the context of an audit and in other engagements to clarify its application.
21. The QCOWG also considered the EQC review in the context of a firm's overall quality management, noting that an EQC review is a control that the firm has available to safeguard against the issuance of an inappropriate engagement report. The QCOWG noted that, absent a requirement to perform an EQC review, and as part of its risk-based approach to managing quality, firms may identify a specific risk for which a response other than, or in addition to, an EQC review may be more appropriate. For example, firms may require engagement teams to consult in situations where the team proposes to set materiality outside of the firm's normal benchmarks. The QCOWG considered that it was important to develop application material that acknowledges an EQC review is part of a firm's overall quality management.

*Proposed Changes to Extant ISQC 1*

22. The proposed changes to the requirement in extant ISQC 1 and its associated application material concerning the identification of engagements that should be subject to an EQC review are as follows:

Requirements

35. The firm shall establish policies and procedures that require an engagement quality control review for all audits of financial statements of listed entities and for all engagements for which an engagement quality control review is required by law or regulation. In addition, the firm shall establish risk-based criteria to identify any other engagements for which an engagement quality control review is required.~~requiring, for appropriate engagements, an engagement quality control review that provides an objective evaluation of the significant judgments made by the engagement team and the conclusions reached in formulating the report. Such policies and procedures shall: In establishing the criteria for other engagements, the firm shall take into account: (Ref: Para. A41)~~
- (a) Entities, other than listed entities, for which the firm performs audits of financial statements and the extent to which such entities have risk characteristics similar to listed entities. (Ref: Para. A41a)~~Require an engagement quality control review for all audits of the financial statements of listed entities;~~
- (b) Risks to quality at the engagement level identified by the firm for which an engagement quality control review is an appropriate response. (Ref: Para. A41b-A41d)~~Set out criteria against which all other audits and reviews of historical financial information and other assurance and related services engagements, firms be~~

~~evaluated to determine whether an engagement quality control review should be performed; and (Ref: Para. A41)~~

- ~~(c) Require an engagement quality control review for all engagements, if any, meeting the criteria established in compliance with subparagraph 35(b).~~

#### Application Material

~~A41. Law or regulation may require an engagement quality control for engagements that meet certain criteria for determining which engagements, other than audits of financial statements of listed entities, are to be subject to an engagement quality control review may include, for example:~~

- ~~• Entities that are determined by the local jurisdiction to be The nature of the engagement, including the extent to which it involves a matter of public interest entities;<sup>5</sup>~~
- ~~• Public sector entities; or~~
- ~~• Entities that operate in certain industries, such as banking, insurance or pension funds.~~
- ~~• The identification of unusual circumstances or risks in an engagement or class of engagements.~~
- ~~• Whether laws or regulations require an engagement quality control review.~~

~~A41a. Similar to listed entities, some entities, by their nature will have a significant impact to the public, if an inappropriate auditor's report was to be issued. Examples of factors to consider in determining whether to require an engagement quality control review for an audit of financial statements because of the nature of the entity include:~~

- ~~• The nature of the business, for example, entities holding assets in a fiduciary capacity for a large number of stakeholders, that offer insurance to the general public, or that are larger charities;~~
- ~~• The size of the entity;~~
- ~~• Entities with a substantial number of employees; or~~
- ~~• Entities that have a large number or a wide range of stakeholders, for example those that operate in the public sector or that are supported by public funding.~~

~~A41b. In developing additional criteria to determine if there are risks specific to an audit engagement, firms may consider:~~

- ~~• Whether the entity is undergoing, or plans to undergo, an initial public offering;~~
- ~~• Previous issues encountered on the engagement such as significant inspection findings, material restatements of comparative information in financial statements or an auditor's report that required reissuance;~~
- ~~• Significant changes in the relevant financial reporting framework including those that would impact significant accounting policies or principles;~~
- ~~• The complexity or level of judgment required for the specific audit; or~~

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<sup>5</sup> It is intended that public interest entities will be in the context of public interest entities defined and used by the local jurisdiction.

- Tenure of senior members of the engagement team, including engagement partners that are new to the position, engagement or industry or engagement partners that have a long association with the entity.

A41c. In developing additional criteria to determine if there are risks specific to an engagement that is not an audit of financial statements, firms may consider:

- The nature of the engagement;
- Whether the firm routinely performs such type of engagements;
- The complexity or level of judgment required for the specific engagement;
- Whether the engagement is one of assurance services for a listed entity with a widely distributed report; and
- Whether the engagement report is widely distributed or concerns a subject matter where expertise other than that of the engagement team is needed.

A41d. In developing the policies to determine for which engagements an engagement quality control review is an appropriate response to quality risks, firms may consider other types of responses it employs, as part of its quality management, to address specific quality risks. For example, when a specific quality risk has been identified, a firm may require reviews of certain areas of an engagement before the report on that engagement is issued, may require the use of certain experts such as the firm's accounting specialists to review the financial statements or report to be issued, or may require consultations on specific quality risk matters arising in an engagement.

#### **Matter for IAASB Consideration**

2. The IAASB is asked for its views on the proposed changes to the requirements and associated application material concerning the scope of engagements that should be subject to an EQC review.

### **Execution of an EQC Review**

#### *Board Discussion*

23. As highlighted above, the Board had the view that the EQC review continue to focus on significant judgments made by the engagement team during the course of the engagement. However, there were differing views among the Board members as to what constituted significant judgments in the context of an engagement. The Board also recommended that further emphasis be placed on the timeliness of the EQC review.

#### *Working Group Discussions*

##### Significant Judgment

24. The QCOWG further considered what matters should be considered significant judgments made by the engagement team in the context of an EQC review and how these could be incorporated into a revised standard.
25. Outreach to firms indicated that the matters reviewed by the EQC reviewer, other than those prescribed by the standard, were often based on discussions between the EQC reviewer and the engagement team. Further, discussions indicated that there is some prescription on the practical application of determining which matters in an engagement were significant and therefore within the scope of the EQC review. Firms also indicated that competence and

capabilities of the engagement team, including the EQC reviewer's experience with the team, are also a consideration in determining the extent of the EQC review. Further detail of these matters is included in paragraph 27 below.

26. The QCOWG performed a search of the ISAs, AS 7, the relevant article of EU Regulation and the guidance issued by the United Kingdom Financial Reporting Council (UKFRC), *Audit Quality Practice Aid for Audit Committees*<sup>6</sup> (the UKFRC Practice Aid), to identify instances where the terms "significant matter" or "significant judgment" are discussed (refer to Appendix 1 for the compilation of these instances). Based on its review of this compilation, the QCOWG noted references in the ISAs to significant matters or significant judgments that are not incorporated in the extant application material for EQC reviews. The QCOWG considered which of these references could be relevant in performing an EQC review and has proposed to include those relevant references in the application material concerning the nature, timing and extent of an EQC review.

#### *Timing of the EQC Review*

27. The QCOWG performed outreach to firms regarding the timing of the EQC review, to determine if their respective methodologies included guidance on when the EQC reviewer should be involved in the audit and at what stages the review procedures should be performed. The QCOWG noted the following guidance:
- EQC reviewers are required to approve the audit planning prior to the commencement of the fieldwork, this may include the following:
    - Audit scoping, including:
      - Scoping group audits;
      - Understanding the entity and its control environment;
      - Determining materiality;
      - The approach to auditing estimates; and
      - The strategy for opening balances on initial engagements.
    - Acceptance and continuance considerations, including independence and engagement terms and the engagement team's assessment of the competence and integrity of management.
    - The risk assessment, including changes in the risk assessment, significant risks and risks associated with accounting estimates.
    - Significant entity specific accounting and auditing issues.
    - Consideration of required consultations and the proposed use of specialists or experts.
    - Fraud considerations, including fraud discussions, the identification of related parties.
    - Going concern issues.

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<sup>6</sup> [https://frc.org.uk/Our-Work/Publications/Audit-and-Assurance-Team/Audit-Quality-Practice-Aid-for-Audit-Committee-\(1\).pdf](https://frc.org.uk/Our-Work/Publications/Audit-and-Assurance-Team/Audit-Quality-Practice-Aid-for-Audit-Committee-(1).pdf)

- The impact of significant changes in accounting or auditing standards, for example, the impact of key audit matters and the scope of other information, resulting from the adoption of the auditor reporting suite of standards.
- Interim procedures – EQC reviewers are required to attend, or review the minutes from, team discussions to discuss the results of interim audit procedures performed and any impact on the initially planned audit strategy.
- EQC reviewers are required to complete and sign off on their review prior to the release of the auditor's report. This review may include the following:
  - Evaluation of significant judgments, including:
    - Significant risks;
    - Consultations;
    - Significant accounting and auditing issues;
    - Going concern;
    - Tax conclusions;
    - Identified misstatements (corrected and uncorrected); and
    - For the audit of groups, conclusions in respect of significant judgments.
  - The financial statements and the associated disclosure checklist.
  - The auditor's report.
  - Written communications with those charged with governance.
  - Independence conclusions
- Some firms also indicated that there was no specific guidance on timing on other involvement and that it was often a collaborative process between the engagement team and the EQC reviewer, while another indicated that quality milestones had been established.

#### *Documentation of the EQC Review*

28. The QCOWG performed outreach to firms in this area to determine if their respective methodologies included guidance on how the EQC review should be documented. The QCOWG noted the following guidance:
- EQC reviewers are required to sign off on all working papers reviewed as part of the EQC review.
  - EQC reviewers have a separate section in the audit file which includes, among other matters, confirmation of the review of relevant documentation, satisfactory resolution of matters identified during the EQC review and concurrence with the issuance of the auditor's report.
29. More specific documentation requirements in respect of the EQC review include:
- Minutes of the EQC reviewer's challenges;
  - Sign off of concurrence with the planned audit strategy, which includes the identification of significant risks, the planned approach to these risks and the engagement team's judgments in relation to materiality;

- Sign off, as evidence of review, of any written communications with those charged with governance in advance of those communications being provided;
- Evidence of the clearance of challenges posed by the EQC reviewer;
- Sign off, as evidence of review, of the engagement completion document that includes the significant matters identified as part of the audit; and
- Completion of programs required at various stages of the engagement that encompass the areas described in paragraph 27.

#### *Working Group Recommendations*

30. In considering revisions to ISQC 1, the QCOWG is cognizant of the responses to the ITC that cautioned against updating requirements and guidance on the scope of the engagement quality review such that it results in a checklist approach to its implementation. Further, the QCOWG is of the view that such an approach would not be consistent with the quality management approach proposed in the ITC and currently being further explored by the Quality Management Approach Working Group (QMAWG).
31. The QCOWG remains of the view that there is support from respondents to the ITC to enhance the requirements and application material addressing the scope of the EQC review and the EQC reviewer's involvement, but notes that any proposed updates need to be scalable,<sup>7</sup> and reflect the concepts of quality management.
32. The QCOWG is further of the view that it should be clear in the standards that the EQC reviewer should be involved in all stages of the audit and therefore suggests that the concepts of paragraph A43 of extant ISQC 1 be promoted to a requirement. This is consistent with the how the timing of the review is reflected in the proposed objective. To reinforce the concept of the involvement of the EQC reviewer at all stages of the engagement, the QCOWG is of the view that the requirement should make specific reference to such stages. The QCOWG determined that the stages encompassing "strategy," "execution" and "conclusion" could be practically applied to all types of engagements.
33. In addition to addressing the timing of the EQC review, the QCOWG considered support from respondents to the ITC and from the Board to further clarify the nature, extent and documentation of the EQC review. The QCOWG is of the view that amending paragraph 36 of extant ISQC 1 and developing additional application material will provide further guidance and clarification for firms in these areas.
34. In respect of the procedures to be performed by the EQC reviewer, the QCOWG considered two alternate structures in developing the proposed requirement(s). The QCOWG had mixed views on which structure was more appropriate. As such, both of these structures are presented below for discussion with the Board (i.e., alternative 1 would comprise two separate paragraphs, 37 and 37a, and alternative 2 would comprise a single paragraph, 37).
35. The QCOWG proposes the following updates to ISQC 1:  

Requirements

  36. ~~The firm's shall establish policies and procedures shall setting out the nature timing and extent of an engagement quality control review. Such policies and procedures shall require~~

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<sup>7</sup> Refer to paragraph 8 of Agenda Item 6–A regarding the use of the terms scalable and proportionate.

~~that the engagement report is not dated until the completion of the engagement quality control review.~~ (Ref: Para: A42-A443)

- ~~(a) The nature of the matters to be considered by the engagement quality control reviewer.~~
- ~~(b) The timing of the review procedures to be performed by the engagement quality control reviewer, including that the procedures be performed at appropriate stages during the engagement.~~
- ~~(c) The extent of the procedures to be performed by the engagement quality control reviewer, that enable the engagement quality control reviewer to conclude on the appropriateness of the judgments made by the engagement team.~~
- ~~(d) The extent of the documentation required to record the performance, results and conclusions of the review performed by the engagement quality control reviewer.~~

Alternative 1

~~37. The firm shall establish policies and procedures to require~~ At a minimum, the engagement quality control review to include ~~or shall perform procedures to evaluate significant judgments, if any, made by the engagement team in relation to:~~ (Ref: Para: A44a-A45a)

- ~~(a) Discussion of significant matters with the engagement partner [included in paragraph 37a below]~~ The strategy, or similar plan, for undertaking the engagement;
- ~~(b) Review of the financial statements or other subject matter information and the proposed report;~~ The execution of the engagement;
- ~~(c) Review of selected engagement documentation relating to significant judgments the engagement team made and the conclusions it reached; and~~
- ~~(d) Evaluation of~~ the overall conclusions reached by the engagement team; and in formulating the report and consideration of whether
- ~~(e) The proposed engagement report is appropriate.~~ (Ref: Para. A44)

37a. The firm's policies and procedures shall require that the engagement quality control reviewer discuss the significant judgments with the engagement partner and evaluate the documentation prepared by the engagement team in relation to the areas selected for review by the engagement quality control reviewer. The review shall include whether the engagement team's documentation reflects the work performed in relation to significant judgments and supports the conclusions reached by the engagement team. (Ref: Para. A45b)

Alternative 2

~~37. The firm's shall establish policies and procedures shall~~ require the engagement quality control reviewer to include:

- ~~(a) Discussion of significant judgments with the engagement partner;~~
- ~~(b) Review of the financial statements or other subject matter information and of the proposed report;~~
- Perform procedures to evaluate significant judgments, if any, made by the

engagement team in relation to: (Ref: Para: A44a-A45a)

(i) The strategy, or similar plan, for undertaking the engagement;

(ii) The execution of the engagement;

(iii) The overall conclusions reached by the engagement team;

(iv) The proposed engagement report.

~~(de) Evaluate the Review of selected engagement documentation prepared by the engagement team in relation to the areas selected for review by the engagement quality control reviewer, including whether the documentation reflects the work performed in relation to significant judgments and supports the conclusions reached by the engagement team. (Ref: Para. A45b) relating to significant judgments the engagement team made and the conclusions it reached; and~~

~~(d) Evaluation of the conclusions reached in formulating the report and consideration of whether the proposed report is appropriate.~~

38. For audits of financial statements ~~of listed entities~~, the firm shall establish policies and procedures ~~to that~~ require the engagement quality control reviewer ~~to consider to also include consideration of the following: (Ref: Para. A45–A46)~~

(a) The engagement team's evaluation of the firm's independence in relation to the specific engagement; and

(b) Whether appropriate consultation has taken place on matters involving differences of opinion or other difficult or contentious matters, and the conclusions arising from those consultations; ~~and~~

~~(c) Whether documentation selected for review reflects the work performed in relation to the significant judgments and supports the conclusions reached. (Ref: Para. A45–A46)~~

#### Application Material

A42. The engagement report is not dated until the completion of the engagement quality control review. However, documentation of the engagement quality control review may be completed after the date of the report.

A43. Conducting the engagement quality control review in a timely manner at appropriate stages during the engagement allows significant matters to be promptly resolved to the engagement quality control reviewer's satisfaction ~~on or before the date of the report~~. However, the performance of an engagement quality control review does not reduce or replace the responsibilities of the engagement partner.

A44. The nature of the matters considered by the engagement quality control reviewer and timing and extent of the engagement quality control review may depend, among other things, on the nature of the engagement, the complexity of the engagement, whether the entity is a listed entity or has characteristics similar to those of a listed entity, and the risks to quality at the engagement level identified by the firm. ~~that the report might not be appropriate in the circumstances. The performance of an engagement quality control review does not reduce the responsibilities of the engagement partner. In determining the appropriate nature, timing and extent of the procedures required, the firm may:~~

- Establish policies and procedures for audits of financial statements of listed entities that require a more extensive review and identify specific matters for the engagement quality control reviewer to consider, for example, those explained in paragraph A45.
- Specify in the policies and procedures matters to be considered by the engagement quality control reviewer that are responsive to the risk factors that have brought about the need for an engagement quality control review. For example, in the case of an engagement quality control review being required where there has been significant changes in the relevant financial reporting framework, such policies and procedures may specify that the engagement quality control reviewer should perform procedures to evaluate significant judgments in relation to the areas impacted by such change.
- Tailor the policies and procedures to address the nature of the engagement taking into consideration the nature and extent of significant judgments that are expected for the type of engagement subject to the engagement quality control review.

A44a. Paragraph 37 establishes the minimum procedures that an engagement quality control reviewer performs as part of the engagement quality control review. Depending on the conclusions drawn by the engagement quality control reviewer on the appropriateness of the significant judgments identified by the engagement team and the adequacy of the engagement team's response, the engagement quality control reviewer may determine that additional areas of the engagement be incorporated into the review.

~~A45. Other matters relevant to evaluating the significant judgments made by the engagement team that may be considered in an engagement quality control review of an audit of financial statements of a listed entity~~For audits of financial statements, significant judgments made during the engagement may include:

- ~~• Significant risks identified during the engagement and the responses to those risks.~~
- Judgments made, particularly with respect to The materiality level(s) determined by the engagement team and significant risks;
- The engagement team's consideration of risks identified through the acceptance and continuance process and proposed responses to those risks;
- The engagement team's risk assessment process, including identification of significant risks, consideration of other risks the engagement team determined did not rise to the level of a significant risk; and the proposed response to the significant risks;<sup>8</sup>
- The engagement team's proposed group audit strategy with respect to the identification of significant components;<sup>9</sup>
- The engagement team's decisions regarding the use of specialists or experts;
- The engagement team's consideration of, and disclosures of, related party transactions;

<sup>8</sup> The QCOWG will continue to monitor the progress of the ISA 315 (Revised) Task Force regarding changes to ISA 315 (Revised), *Identifying and Assessing the Risks of Material Misstatement through Understanding the Entity and Its Environment*, in relation to the identification of risks, including significant risks and the spectrum of risks.

<sup>9</sup> The QCOWG will continue to monitor the progress of the Group Audits Working Group, in particular as it relates to the identification of components.

- Conclusions drawn, or results of the procedures performed by the engagement team on significant areas of the engagement, for example, conclusions in respect of certain estimates, accounting policies, or going concern considerations;
- The engagement team's evaluation of the procedures performed by experts and conclusions drawn therefrom;
- In group audit situations, the engagement team's evaluation of work performed by component auditors and the conclusions drawn therefrom;
- The significance and disposition of corrected and uncorrected misstatements identified during the engagement;
- The engagement team's proposed audit opinion and matters to be communicated in the auditor's report, for example, key audit matters, or a "Material Uncertainty Related to Going Concern" paragraph; or
- The matters to be communicated to management and those charged with governance and, where applicable, other parties such as regulatory bodies.

~~These other matters, depending on the circumstances, may also be applicable for engagement quality control reviews for audits of the financial statements of other entities as well as reviews of financial statements and other assurance and related services engagements.~~

A45a. For engagements other than audits of financial statements, some of the significant judgments identified in paragraph A45 may be relevant, for example, judgments with respect to materiality and the engagement team's decision regarding the use of specialists and experts. There may also be other significant judgments in relation to the engagement, for example, in the case of an assurance engagement performed in accordance with ISAE 3000 (Revised),<sup>10</sup> significant judgment may include the engagement team's determination of whether the criteria to be applied in the preparation of the subject matter information are suitable for the engagement circumstances.

A45b. The documentation that the engagement quality control reviewer selects for review includes documentation concerning the significant judgments made by the engagement team. This may include:

- Documentation of the planned engagement strategy;
- Selected working papers concerning certain areas of significant judgments;
- Summaries of identified corrected and uncorrected misstatements;
- Documentation or a summary of engagement findings;
- Communications with management or those charged with governance as applicable;
- The engagement report and any associated checklist.

Depending on the circumstances and the type of engagement being performed, the review of other documentation may be appropriate.

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<sup>10</sup> ISAE 3000 (Revised), *Assurance Engagements Other than Audits or Reviews of Historical Financial Information*

**Matters for IAASB Consideration**

3. The IAASB is asked:
  - (a) For its views on the proposed enhancements to the requirements in ISQC 1 addressing the nature, timing and extent of the EQC review, including the proposed amendments to the application material; and
  - (b) Whether it prefers proposed requirements addressing the procedures to be performed by the EQC reviewer to be presented as two separate paragraphs (i.e., alternative 1 represented in paragraph 37 and 37a) or as a single paragraph (i.e., alternative 2 represented in paragraph 37).

## Appendix 1

### Comparison of Sources Referencing Significant Matter or Significant Judgment

This Appendix is presented for informational purposes only. It is a compilation of the references to significant matters and significant judgments in the ISAs, AS 7, the UKFRC Practice Aid and the EU Regulation that were identified by the QCOWG and used for reference in the development of certain application material contained within the Agenda Item.

#### International Standards on Auditing

##### ISA 220, *Quality Control for an Audit of Financial Statements*

A18. Timely reviews of the following by the engagement partner at appropriate stages during the engagement allow significant matters to be resolved on a timely basis to the engagement partner's satisfaction on or before the date of the auditor's report:

- Critical areas of judgment, especially those relating to difficult or contentious matters identified during the course of the engagement;
- Significant risks; and
- Other areas the engagement partner considers important.

...

A28. Other matters relevant to evaluating the significant judgments made by the engagement team that may be considered in an engagement quality control review of a listed entity include:

- Significant risks identified during the engagement in accordance with ISA 315 (Revised),<sup>11</sup> and the responses to those risks in accordance with ISA 330,<sup>12</sup> including the engagement team's assessment of, and response to, the risk of fraud in accordance with ISA 240.<sup>13</sup>
- Judgments made, particularly with respect to materiality and significant risks.
- The significance and disposition of corrected and uncorrected misstatements identified during the audit.
- The matters to be communicated to management and those charged with governance and, where applicable, other parties such as regulatory bodies.

These other matters, depending on the circumstances, may also be applicable for engagement quality control reviews for audits of financial statements of other entities.

##### ISA 230, *Audit Documentation*

A8. Judging the significance of a matter requires an objective analysis of the facts and circumstances. Examples of significant matters include:

- Matters that give rise to significant risks (as defined in ISA 315 (Revised)).

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<sup>11</sup> ISA 315 (Revised), *Identifying and Assessing the Risks of Material Misstatement through Understanding the Entity and Its Environment*

<sup>12</sup> ISA 330, *The Auditor's Responses to Assessed Risks*

<sup>13</sup> ISA 240, *The Auditor's Responsibilities Relating to Fraud in an Audit of Financial Statements*

- Results of audit procedures indicating (a) that the financial statements could be materially misstated, or (b) a need to revise the auditor’s previous assessment of the risks of material misstatement and the auditor’s responses to those risks.
  - Circumstances that cause the auditor significant difficulty in applying necessary audit procedures.
  - Findings that could result in a modification to the audit opinion or the inclusion of an Emphasis of Matter paragraph in the auditor’s report.
- A9. An important factor in determining the form, content and extent of audit documentation of significant matters is the extent of professional judgment exercised in performing the work and evaluating the results. Documentation of the professional judgments made, where significant, serves to explain the auditor’s conclusions and to reinforce the quality of the judgment. Such matters are of particular interest to those responsible for reviewing audit documentation, including those carrying out subsequent audits when reviewing matters of continuing significance (for example, when performing a retrospective review of accounting estimates).
- A10. Some examples of circumstances in which, in accordance with paragraph 8, it is appropriate to prepare audit documentation relating to the use of professional judgment include, where the matters and judgments are significant:
- The rationale for the auditor’s conclusion when a requirement provides that the auditor “shall consider” certain information or factors, and that consideration is significant in the context of the particular engagement.
  - The basis for the auditor’s conclusion on the reasonableness of areas of subjective judgments (for example, the reasonableness of significant accounting estimates).
  - The basis for the auditor’s conclusions about the authenticity of a document when further investigation (such as making appropriate use of an expert or of confirmation procedures) is undertaken in response to conditions identified during the audit that caused the auditor to believe that the document may not be authentic.
- A11. The auditor may consider it helpful to prepare and retain as part of the audit documentation a summary (sometimes known as a completion memorandum) that describes the significant matters identified during the audit and how they were addressed, or that includes cross-references to other relevant supporting audit documentation that provides such information. Such a summary may facilitate effective and efficient reviews and inspections of the audit documentation, particularly for large and complex audits. Further, the preparation of such a summary may assist the auditor’s consideration of the significant matters. It may also help the auditor to consider whether, in light of the audit procedures performed and conclusions reached, there is any individual relevant ISA objective that the auditor cannot achieve that would prevent the auditor from achieving the overall objectives of the auditor.

ISA 260 (Revised), *Communication with Those Charged With Governance*

16. The auditor shall communicate with those charged with governance: (Ref: Para. A17–A18)
- (a) The auditor’s views about significant qualitative aspects of the entity’s accounting practices, including accounting policies, accounting estimates and financial statement disclosures....
- ...
- (c) ...

- (i) Significant matters arising during the audit that were discussed, or subject to correspondence, with management; and (Ref: Para. A22)
- (ii) ...

...

- (e) Any other significant matters arising during the audit that, in the auditor's professional judgment, are relevant to the oversight of the financial reporting process. (Ref: Para. A26–A28)
- A20. As a result, the auditor's views on the subjective aspects of the financial statements may be particularly relevant to those charged with governance in discharging their responsibilities for oversight of the financial reporting process. For example, in relation to the matters described in paragraph A19, those charged with governance may be interested in the auditor's evaluation of the adequacy of disclosures of the estimation uncertainty relating to accounting estimates that give rise to significant risks. Open and constructive communication about significant qualitative aspects of the entity's accounting practices also may include comment on the acceptability of significant accounting practices and the quality of the disclosures. Appendix 2 identifies matters that may be included in this communication.
- A22. Significant matters discussed, or subject to correspondence with management may include such matters as:
- Significant events or transactions that occurred during the year.
  - Business conditions affecting the entity, and business plans and strategies that may affect the risks of material misstatement.
  - Concerns about management's consultations with other accountants on accounting or auditing matters.
  - Discussions or correspondence in connection with the initial or recurring appointment of the auditor regarding accounting practices, the application of auditing standards, or fees for audit or other services.
  - Significant matters on which there was disagreement with management, except for initial differences of opinion because of incomplete facts or preliminary information that are later resolved by the auditor obtaining additional relevant facts or information.
- A26. ISA 300<sup>14</sup> notes that, as a result of unexpected events, changes in conditions, or the audit evidence obtained from the results of audit procedures, the auditor may need to modify the overall audit strategy and audit plan and thereby the resulting planned nature, timing and extent of further audit procedures, based on the revised consideration of assessed risks. The auditor may communicate with those charged with governance about such matters, for example, as an update to initial discussions about the planned scope and timing of the audit.
- A27. Other significant matters arising during the audit that are directly relevant to those charged with governance in overseeing the financial reporting process may include such matters as material misstatements of the other information that have been corrected.
- A49. Timely communication throughout the audit ... Relevant circumstance include the significance and nature of the matter, and the action expected to be taken by those charged with governance. For example:

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<sup>14</sup> ISA 300, *Planning an Audit of Financial Statements*, paragraph A13

- ...
- Communications regarding independence may be appropriate whenever significant judgments are made about threats to independence and related safeguards, for example, when accepting an engagement to provide non-audit services, and at a concluding discussion.

...

ISA 315 (Revised), *Identifying and Assessing the Risk of Material Misstatement Through Understanding the Entity and Its Environment*

A134. Risks of material misstatement may be greater for significant judgmental matters that require the development of accounting estimates, arising from matters such as the following:

- Accounting principles for accounting estimates or revenue recognition may be subject to differing interpretation.
- Required judgment may be subjective or complex, or require assumptions about the effects of future events, for example, judgment about fair value.

ISA 550, *Related Parties*

A50. Communicating significant matters arising during the audit<sup>15</sup> in connection with the entity's related parties ... Examples of significant related party matters include:

- Non-disclosure (whether intentional or not) by management to the auditor of related parties or significant related party transactions, which may alert those charged with governance to significant related party relationships and transactions of which they may not have been previously aware.
- The identification of significant related party transactions that have not been appropriately authorized and approved, which may give rise to suspected fraud.
- Disagreement with management regarding the accounting for and disclosure of significant related party transactions in accordance with the applicable financial reporting framework.
- Non-compliance with applicable law or regulations prohibiting or restricting specific types of related party transactions.
- Difficulties in identifying the party that ultimately controls the entity.

ISA 570 (Revised), *Going Concern*

A23. ...Disclosures required by some financial reporting frameworks that are in addition to matters set forth in paragraph 19 may include disclosures about:

- ...
- Significant judgments made by management as part of its assessment of the entity's ability to continue as a going concern.

...

ISA 610 (Revised 2013), *Using the Work of Internal Auditors*

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<sup>15</sup> ISA 230, *Audit Documentation*, paragraph A8, provides further guidance on the nature of significant matters arising during the audit.

A19. Since the external auditor has sole responsibility for the audit opinion expressed, the external auditor needs to make the significant judgments in the audit engagement in accordance with paragraph 18. Significant judgments include the following:

- Assessing the risks of material misstatement;
- Evaluating the sufficiency of tests performed;
- Evaluating the appropriateness of management's use of the going concern assumption;
- Evaluating significant accounting estimates; and
- Evaluating the adequacy of disclosures in the financial statements, and other matters affecting the auditor's report.

IAPN 1000, *Special Considerations in Auditing Financial Instruments*

102. Areas of more significant judgment are often tested close to, or at, the period end as:

- Valuation can change significantly in a short period of time, making it difficult to compare and reconcile interim balances with comparable information at the balance sheet date;
- An entity may engage in an increased volume of financial instrument transactions between an interim period and year-end;
- Manual journal entries may only be made after the end of the accounting period; and
- Non-routine or significant transactions may take place late in the accounting period.

#### **PCAOB – AS 7, *Engagement Quality Control Reviews***

10. In an audit, the engagement quality reviewer should:

- a. Evaluate the significant judgments that relate to engagement planning including-
  - The consideration of the firm's recent engagement experience with the company and risk identified in connection with the firm's client acceptance and retention process.
  - The consideration of the company's business, recent significant activities, related financial reporting issues and risks, and
  - The judgments made about materiality and the effect of those judgments on the engagement strategy
- b. Evaluate the engagement team's assessment of and audit responses to-
  - Significant risks identified by the engagement team, including fraud risks, and
  - Other significant risks identified by the engagement quality reviewer through performance of the procedures required by this standard.
- c. Evaluate the significant judgments made about (1) the materiality and disposition of corrected and uncorrected identified misstatements and (2) the severity and disposition of identified control deficiencies.

...

#### **UKFRC Practice Aid**

4.7 In summary, the auditor's judgments made in an audit include judgments about:

- Materiality;

- The auditor's risk assessment;
- The auditor's response – the nature timing and extent of further audit procedures (scope); and;
- The auditor's conclusions and reporting – based on their evaluations.

**EU Regulation Article 8(5)**

The review shall at least assess the following elements:

- (a) the independence of the statutory auditor or the audit firm from the audited entity;
- (b) the significant risks which are relevant to the statutory audit and which the statutory auditor or the key audit partner has identified during the performance of the statutory audit and the measures that he or she has taken to adequately manage those risks;
- (c) the reasoning of the statutory auditor or the key audit partner, in particular with regard to the level of materiality and the significant risks referred to in point (b);
- (d) any request for advice to external experts and the implementation of such advice;
- (e) the nature and scope of the corrected and uncorrected misstatements in the financial statements that were identified during the carrying out of the audit;
- (f) the subjects discussed with the audit committee and the management and/or supervisory bodies of the audited entity;
- (g) the subjects discussed with competent authorities and, where applicable, other third parties;
- (h) whether the documents and information selected from the file by the reviewer support the opinion of the statutory or key audit partner as expressed in the draft of the reports referred to in Articles 10 and 11 [the audit report and the additional report to the audit committee].

## Appendix 2

### Minutes – IAASB September 2016 Meeting<sup>16</sup>

Ms. French introduced the topic of engagement quality control (EQC) reviews and provided an overview of the CAG Representatives views in respect of the issues presented in **Agenda Item 5-B**. Ms. French noted that CAG Representatives were supportive of strengthening the requirements for engagements that should be subject to an EQC review, although had mixed views about how this should be operationalized. Furthermore, the CAG agreed that an objective should be established, however had diverse views regarding the depth of the EQC review and whether it should remain focused on significant judgments. CAG Representatives also emphasized the importance of the timeliness of the EQC review, and the selection of an EQC reviewer with the appropriate competencies, authority and independence, noting the importance of the firm's tone and culture towards the EQC review. There were also varied views by CAG Representatives regarding providing transparency about the EQC review in the auditor's report.

Ms. French provided feedback from the SMP Committee, noting the caution for the IAASB in extending the requirement for an EQC review beyond listed entities to include all public interest entities and supporting the determination of an objective for the EQC review. In addition, Ms. French noted that the SMP Committee also noted that further consideration be given to aspects of the eligibility of the EQC reviewer. The Board provided the Quality Control Working Group (QCWG) with further direction, as set out in the sections below, to address respondent's feedback to the ITC.

#### EXTENDING THE REQUIREMENT FOR AN EQC REVIEW BEYOND AUDITS OF LISTED ENTITIES

The Board agreed that the requirement for an EQC review needs to be strengthened, with broad support for the firm to determine which engagements should be subject to an EQC review on the basis of a risk-based approach supported by robust criteria (i.e., in addition to listed entities or those required by law or regulation to be subject to an EQC review). The Board provided the following additional suggestions and matters for consideration:

- Any changes should address the fundamental reason why the EQC review requirement should be extended, i.e., to address the impact of a possible audit failure, specifically the public interest impact.
- Further consideration should be given to how the quality management approach will also help signal engagements where an EQC review should be performed.
- The EQC review requirements should be addressed in a manner that does not undermine other responses implemented by the firm to address quality risks. Recognition of other forms of reviews that are not strictly EQC reviews may also be appropriate to facilitate more focused reviews on engagements, or areas of those engagements, where risk exists.
- The criteria should not be prescriptive and ought to focus on the public interest aspects (including entities that utilize funds from the public or government). The Board provided some suggestions of possible criteria.
- Appropriate emphasis to circumstances where jurisdictions prescribe entities that should be subject to EQC review, which could encourage jurisdictions to make such a determination.

<sup>16</sup> These draft minutes are still subject to IAASB review and may be subject to further change.

#### OBJECTIVE OF THE EQC REVIEW

The Board agreed that the EQC review is a firm level control performed at the engagement level, given the purpose of the EQC review in responding to risks at the firm level and the determination being made by the firm of which engagements are subject to EQC reviews. Furthermore, the Board was of the view that the responsibility for audit quality at the engagement level rests with the engagement partner, and setting the objective as an engagement level control could dilute this responsibility. In establishing the objective, the Board requested that the QCWG further consider:

- Clearly articulating the level at which the control is established in order to make clear where accountability is, while also explaining the nature, timing and extent in performing the EQC review at the engagement level in ISA 220.
- As it relates to the depth of the review, retaining the focus on significant judgments made by the engagement team, although providing clarity about what this means. Ms. Healy recommended that paragraphs A8 to A11 of ISA 230<sup>17</sup> could also be helpful in considering the meaning of “significant judgments.”
- Emphasizing that the EQC review is an activity that should take place throughout the engagement, and not merely be performed at the end of the engagement.
- How to link quality management at the engagement level and the EQC review (i.e., the quality management at the engagement level would facilitate improved information for the engagement partner to engage throughout the audit with the EQC reviewer).

#### SELECTION OF THE EQC REVIEWER

The Board supported the recommendations of the QCWG as they relate to improving the robustness of the selection of the EQC reviewer, although cautioned that these should not be overly prescriptive resulting in firms having limited suitable resources who are able, or willing, to fulfill the role. The Board was of the view that the selection of the EQC reviewer should be at firm level, rather than the engagement level, given that the EQC review is a firm level control. The Board provided the following additional matters for consideration:

- Emphasizing that the EQC reviewer should have the appropriate authority and status within the firm to enable them to confidently challenge the significant judgments.
- Addressing the appropriateness of the EQC reviewer’s practical experience, for example, circumstances when the EQC review is delegated to a technical resource with limited practical experience.
- Reinforcing that the function of the EQC reviewer is not to override the judgments of the engagement team, but rather for the EQC reviewer to challenge those judgments and for the engagement team to evaluate how best to address the issues raised by the EQC reviewer.
- Addressing the capacity of the EQC reviewer to perform the review, i.e., their time available.
- Carefully addressing the appropriate skills of the EQC reviewer.

The Board was supportive of further liaison with the IESBA on the issue relating to the ‘cooling-off’ period between serving as the engagement partner and the EQC reviewer, although mixed views were expressed regarding whether a prescriptive period should be established. Those in support of a fixed period suggested 3 years or 5 years and indicated that it would prevent inconsistent application

<sup>17</sup> ISA 230, *Audit Documentation*

by firms, whereas those not supportive of a fixed period were of the view that there is no proper basis for establishing a fixed period.

#### TRANSPARENCY AND INTERACTIONS WITH THOSE CHARGED WITH GOVERNANCE (TCWG)

The Board agreed that transparency in the auditor's report about the engagement being subject to an EQC review would not be appropriate, in particular due to the possible misconceptions it could create about the quality of engagements not subject to EQC reviews. However, the Board had the view that it is important to provide transparency more generally about when an EQC review is performed, to enhance stakeholders' trust and confidence in the audit, in particular given that firms would be making the determination of which engagements should be subject to EQC review (other than for listed entities or as required by law or regulation). Ms. Healy noted that firms' transparency reporting has still yet to be considered by the Board.

The Board was also supportive of the QCWG's conclusion that it would not be appropriate to address the EQC reviewer's interactions with TCWG. The Board further debated the appropriateness of providing transparency to TCWG about the EQC review, recognizing that this information may only be perceived as useful in certain jurisdictions, and encouraged the QCWG to explore how to address the interactions between TCWG and the auditor in the interest of understanding the process of EQC reviews.

#### IAASB CAG CHAIRMAN'S REMARKS

Mr. Waldron noted that the EQC review is a topic that is important to CAG Representatives and generated mixed views and significant interest for some. He highlighted the importance of taking into consideration how the EQC reviewer is assigned, as well as the network's role in EQC reviews, where applicable. Mr. Waldron specifically noted the CAG's comments about the importance of the timing of when the EQC review is undertaken.

#### WAY FORWARD

The QCWG will consider the Board's comments in further developing changes to EQC reviews, and will present their further recommendations to the Board at its December 2016 meeting on the matters discussed at the September 2016 meeting, as well as the nature, timing and extent of the EQC review.