

Proposed ISQM 2¹ – Matters Related to Engagements Subject to an Engagement Quality Review

Objective of the IAASB Discussion

To obtain IAASB views on the proposed wording for paragraph 43(e) of proposed ISQM 1,² and related application material, regarding the scope of engagements for which an engagement quality review would be required in accordance with proposed ISQM 2.

Introduction

1. **Agenda Item 1-A** includes paragraph 43(e) from the extract of proposed ISQM 1, marked for changes from **Supplement C to Agenda Item 6**, which was discussed by the IAASB on September 21, 2018. The application material paragraphs in **Agenda Item 1-A** have been marked for changes from **Supplement C** (paragraphs A100 and A103) or from **Agenda Item 6-B** from the September meeting. A clean version of the updated extract of proposed ISQM 1 has been provided as **Agenda Item 1-B**.
2. In connection with the discussion of proposed ISQM 2 at its September 2018 meeting, the IAASB discussed the requirement and related application material to be included in proposed ISQM 1 relating to engagements to be subject to an engagement quality review (EQR). Among other matters, the IAASB discussed:
 - The requirement for an EQR to be performed for audits of financial statements of entities that the firm determines are of “significant public interest” (SPI) and the related criteria for making that determination (and whether the criteria should be included in the requirement or remain in application material).
 - Whether the requirement for an EQR for audits of entities that are of SPI should be a separate requirement or a subset of engagements for which the firm determines that an EQR is an appropriate response to a quality risk.
 - The examples of engagements for which the firm may determine that an EQR is an appropriate response to a quality risk, including whether the examples are appropriate and reflect engagements relating to financial and non-financial information (i.e., both audit and other engagements).
 - The application material relating to public sector engagements, including factors to consider in determining whether a public sector entity is of SPI.
3. The ISQM 2 Task Force (the Task Force) has considered the comments from the IAASB during the September 2018 meeting, as well as written comments received during and subsequent to the meeting. The Task Force believes that the changes shown in **Agenda Item 1-A** appropriately respond to comments received relating to the engagements to be subject to an EQR. The next section of this paper provides a brief summary of the changes to paragraph 43(e) of proposed ISQM 1, and related application material, to address the Board's comments.

¹ Proposed International Standard on Quality Management (ISQM) 2, *Engagement Quality Reviews*

² Proposed ISQM 1 (previously International Standard on Quality Control 1), *Quality Management for Firms that Perform Audits or Reviews of Financial Statements, or Other Assurance or Related Services Engagements*

Summary of Changes Made

4. The introductory wording to paragraph 43(e) of proposed ISQM 1 has been revised to reflect the wording based on the options discussed by the IAASB at the September 2018 meeting. Of the two options presented by the Task Force, the IAASB expressed a clear preference for Option B (see **Supplement B to Agenda Item 6** for the September meeting). Under this option, proposed ISQM 1 would include a requirement for the firm to establish policies or procedures addressing EQRs to be performed in accordance with proposed ISQM 2, including the engagements for which an EQR would be required. The requirements for the eligibility of the engagement quality reviewer and related performance requirements would reside in proposed ISQM 2. The Task Force will further discuss the split between proposed ISQM 1 and ISQM 2 at its physical meeting in October. Accordingly, the introductory wording proposed for paragraph 43(e) in **Agenda Item 1-A** is subject to change based on that discussion.
5. Other significant revisions in **Agenda Item 1-A**, and the Task Force rationale for the change (or not making a change), are as follows:
 - The Task Force supported the suggestion made at the Board meeting that the requirement for an EQR to be performed for audits of financial statements of entities that the firm determines are of SPI should remain separate to give it increased prominence in view of its importance to the public interest -- see paragraph 43(e)(ii).
 - In light of the revisions proposed to paragraph 43(e) of proposed ISQM 1 as a result of the IAASB's preference for Option B as discussed in paragraph 4 above, the Task Force proposes to move paragraph A99 to proposed ISQM 2.
 - Paragraph A100 is largely consistent with the wording presented to the Board in **Supplement C to Agenda Item 2** at the September 2018 meeting, but has been revised slightly to eliminate multiple uses of 'may' as suggested during the Board meeting. The Task Force also discussed whether the 'criteria' should be included in the requirement in paragraph 43(e)(ii), and concluded that doing so would make the requirement lengthy and more complicated.
 - Paragraph A101 has been restructured and the examples revised in response to written comments received. In particular, related points have been grouped together and examples have been provided for other types of engagements (other than audit engagements) for which the firm may determine that an EQR is an appropriate response to a quality risk.
 - Paragraph A102A has been separated from paragraph A102 in response to a written comment that it is important to emphasize that there may be no engagements for which an EQR is required, or determined to be an appropriate response to a quality risk. The Task Force agreed and also noted that this is separate from the point in paragraph A102 that other types of engagement reviews may be performed.
 - The Task Force noted the support from the IAASB at the September 2018 meeting for the application material relating to the public sector in paragraph A103. The guidance has been further revised and clarified based on written comments received. It has been split into two paragraphs that deal separately with factors to consider in determining whether a public sector entity is of SPI (paragraph A103) and when the firm may determine that an EQR is an appropriate response to a quality risk for engagements in the public sector (paragraph A103A). The Task Force plans to seek input on this application material from INTOSAI representatives prior to the Board teleconference.

Request for Input from the IAASB

6. The Task Force seeks the IAASB's views on the proposed changes for the purpose of closing off the discussion on these paragraphs. However, as noted in paragraph 4 above, the Task Force recognizes that further discussion may be needed on the introductory wording to the requirement in paragraph 43(e).
7. During the Board teleconference, each IAASB member will be called on in turn, and will be asked to provide comments on matters of substance relating to the proposed changes in **Agenda Item 1-A**. There will be a second round of comments to allow Board members, if they so choose, to reflect and provide further input on comments made by others.

Matter for IAASB Consideration

The IAASB is asked for its views on the proposed changes to paragraph 43(e) of proposed ISQM 1, and the related application material, as presented in **Agenda Item 1-A**.