ISSUES PAPER
Proposed ISA 220 (Redrafted) and ISQC 1 (Redrafted)

Introduction
1. This paper summarizes significant matters raised by IAASB at its June 2008 meeting on the proposed revised drafts of ISA 220 (Redrafted)\(^1\) and ISQC 1 (Redrafted)\(^2\), and how the Task Force recommends they be addressed.

2. This paper is structured as follows:

   - **Section A** – Issues where the IAASB reached a conclusion at its June 2008 meeting and provided the Task Force with direction as to their disposition.
   - **Section B** – Matters discussed at the June IAASB meeting which the IAASB asked the Task Force to consider further.
   - **Section C** – Issues unique to ISQC 1 (Redrafted) not covered in Sections A and B.
   - **Section D** – Other drafting changes made to improve the clarity of the proposed standards.
   - **Section E** – Re-exposure considerations.

**SECTION A – ISSUES AGREED AT THE JUNE 2008 IAASB MEETING**

A.1 **LINKAGE BETWEEN ISA 220 AND ISQC 1**

3. The Task Force’s June version of proposed ISA 220 (Redrafted) moved all references to ISQC 1 (Redrafted) to the application material, as some respondents to the exposure draft (“ED-ISA 220”) commented that not all jurisdictions that adopt ISAs will also adopt ISQC 1. At its June meeting, the IAASB stated that a strong link between ISA 220 (Redrafted) and ISQC 1 (Redrafted) is essential; ISA 220 (Redrafted) is not meant to stand-alone and its effectiveness is based on ISQC 1.

**Task Force Recommendations**

4. The Task Force recommends the following approach to link ISA 220 (Redrafted) and ISQC 1 (Redrafted):

   - Include in the Introduction to ISA 220 (Redrafted) two new paragraphs that explain the relationship between the firm’s system of quality control and quality control at the engagement level;
   - Explain that ISA 220 (Redrafted) is premised on the condition that the firm has established and maintains an appropriate system of quality control and that such a system would be one that complies with ISQC 1 (Redrafted), or is based on relevant

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\(^1\) Proposed ISA 220 (Redrafted), “Quality Control for an Audit of Financial Statements.”

\(^2\) Proposed ISQC 1 (Redrafted), “Quality Control for Firms that Perform Audits and Reviews of Financial Statements, and Other Assurance Engagements and Related Services Engagements.”
national requirements that impose obligations on that firm that achieve the aims of the requirements set out in ISQC 1 (Redrafted) (This drafting is intended to accommodate jurisdictions that may not adopt ISQC 1, while ensuring that there is an appropriate quality control system in place in support of quality control at the engagement level. The suggested wording draws from ISA 200 (Revised and Redrafted) and ISA 230 (Redrafted) in relation to their requirements addressing departure from a requirement); and

- Include as application material a summary of the elements of a firm’s system of quality control as set out in ISQC 1 (Redrafted).

See paragraphs 2, 3 and A1 of ISA 220 (Redrafted) in Agenda Item 10-B.

A.2 OBJECTIVE IN ISA 220

5. The Task Force’s June version of proposed ISA 220 (Redrafted) removed the term “reasonable assurance” in the stated objective, as some respondents found the term ambiguous in relation to how it is used elsewhere in the ISAs. At its June meeting, the IAASB reaffirmed its view that the concept of reasonable assurance is appropriate in the objective, as it clarifies in part that absolute assurance at the engagement level is not required.

Task Force Recommendations

6. The Task Force remains concerned that the wording in ED-ISA 220 could be confused with the objective of an auditor in obtaining reasonable assurance as it relates to the audit, as suggested by some of the respondents to the ED.

7. The Task Force has therefore reintroduce the term “reasonable assurance” in the objective in proposed ISA 220 (Redrafted) (as instructed by the IAASB), and proposes to further redraft the objective to make it clear to what the term “reasonable assurance” relates. The revised wording parallels the structure of the objective stated in proposed ISQC 1 (Redrafted).

See paragraph 8 of ISA 220 (Redrafted) in Agenda Item 10-B.

A.3 DATE OF COMPLETION OF ENGAGEMENT QUALITY CONTROL REVIEW (“EQCR”)

8. In developing ED-ISA 220, the IAASB agreed to change the date of completion of an EQCR from the extant “date of report issuance” to “date of auditor’s report” to align proposed ISA 220 (Redrafted) with extant ISA 700.3 The same change was applied to proposed ISQC 1 (Redrafted). The Task Force’s June version of the standards, however, reverted to the wording of extant ISA 220 and ISQC 1 as a number of respondents cited practical issues with IAASB’s proposed change.

9. At its June meeting, the IAASB noted that ISA 700 requires the auditor’s report to be dated no earlier than the date on which the auditor has obtained sufficient appropriate audit

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evidence on which to base the auditor’s opinion on the financial statements. As completion of an EQCR is part of obtaining sufficient appropriate audit evidence, the IAASB reaffirmed its view that it would be inappropriate for the EQCR to be completed after the date of the auditor’s report.

**Task Force Recommendations**

10. The Task Force agrees with IAASB’s position. However, it believes that additional guidance is necessary to help the auditor understand how to apply the standards using the date of the auditor’s report as the date of completion for the EQCR. Accordingly, the Task Force recommends the following:

- To use “date of auditor’s report” as the completion date of an EQCR rather than “issuance date;” and
- To include guidance in the application material to help auditors deal with the practical aspects of the date of report in relation to the completion of an EQCR. In proposed ISA 220 (Redrafted), a link to proposed ISA 700 (Redrafted) is also included to explain why the EQCR must be completed on or before the date of the auditor’s report.

See paragraphs 9(b), 21(c), 27(b), A19, and A23-A25 of ISA 220 (Redrafted) in Agenda Item 10-B.
See paragraphs 12(d), 36, 42(b), 44(b), A41-A42 of ISQC 1 (Redrafted) in Agenda Item 10-E.

**A.4 Definition of Engagement Quality Control Reviewer**

11. The EDs of the proposed standards included the phrase “none of whom is part of the engagement team” in the definition of “engagement team.” The IAASB introduced this phrase as it believes that it clarifies the extant standards which require the engagement quality control reviewer to be objective. The Task Force’s June version of the proposed standards, however, removed this phrase as some respondents stated different interpretations of whether the engagement quality control reviewer can be part of the engagement team under the extant standards.

**Task Force Recommendations**

12. At its June meeting, the IAASB confirmed its opinion that an engagement quality control reviewer could not perform an objective review if the reviewer was a member of the engagement team. The Task Force has therefore re-instated the phrase.

See paragraph 9(c) of ISA 220 (Redrafted) in Agenda Item 10-B.
See paragraph 12(e) of ISQC 1 (Redrafted) in Agenda Item 10-E.

**A.5 Relevant Ethical Requirements – ISA 220 (Redrafted), Paragraph 11**
15. At the June IAASB meeting, a point was raised that the phrase “shall be satisfied” in paragraph 11 of the June version of proposed ISA 220 (Redrafted) is too vague and potentially onerous.

Task Force Recommendations

16. The Task Force has reverted to the wording of ED-ISA 220, including reinstating bullet points (a) and (b) to the requirements section to support the “evaluation” requirement.

See paragraph 11 of ISA 220 (Redrafted) in Agenda Item 10-B.

A.6 DETERMINING THE SUFFICIENCY OF MEASURES TAKEN BY THE FIRM TO RECTIFY DEFICIENCIES FOUND IN THE MONITORING PROCESS

17. At the June IAASB meeting, a point was raised that the proposed requirement for the engagement partner to determine whether measures taken by the firm to rectify deficiencies are sufficient in the context of the audit engagement may imply that the engagement partner needs to ‘second-guess’ measures taken by the firm to rectify the situation.

18. The Task Force has revised with wording of paragraph 25 of ISA 220 (Redrafted) to require the engagement partner to evaluate whether deficiencies noted in the results of the monitoring that have not been rectified by the firm would affect the audit.

See paragraph 25 of ISA 220 (Redrafted) in Agenda Item 10-B.

A.7 SMP ISSUES

19. At the June IAASB meeting, concern was raised that auditors may still be unclear that, in some cases, none of a firm’s engagements may meet the criteria that would subject them to an EQCR.

20. The Task Force believes that further guidance material in ISA 220 (Redrafted) would assist in making this point clear. In addition, the Task Force has further clarified in the application material when the requirements of proposed ISQC 1 (Redrafted) would not apply in a small-and medium-sized practice (SMP) environment.

See paragraph A29 of ISA 220 (Redrafted) in Agenda Item 10-B.
See paragraph A1 of ISQC 1 (Redrafted) in Agenda Item 10-E.

SECTION B – MATTERS FOR FURTHER CONSIDERATION

B.1 DEFINITION OF “FIRM”

21. ED-ISA 220 and ED-ISQC 1 retained the definition of “firm” as per the extant equivalents.\(^4\) The Task Force’s June version of the revised draft of these standards, however, proposed that the definition be amended to align it with that in the IFAC Code.\(^5\)

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\(^4\) Extant ISA 220 and ISQC 1 define the firm as “a sole practitioner, partnership or corporation or other entity of professional accountants.”

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22. Some IAASB members were concerned that the proposed change in definition (to that of the IFAC Code) had not been exposed, as well as about possible unintended consequences arising from the change. The IAASB asked the Task Force to determine the effect of adopting the IFAC Code’s definition of “firm” in ISA 220 (Redrafted) and ISQC 1 (Redrafted).

Task Force Recommendations

23. The Task Force recommends that the definition of firm in the extant ISA 220 and ISQC 1 be retained (as per ED-ISA 220 and ED-ISQC 1). This reinforces the point that there is no intention to expand the scope of the quality control standards in the process of redrafting them. Further, it avoids any potential unintended consequences; though the Task Force does not believe there would be, it cannot give the IAASB assurance to this effect. Finally, it reflects the fact that the IESBA definition is designed specifically for purposes of compliance with ethical requirements, in particular independence, whereas the extant ISA 220 and ISQC 1 definition is suitable for purposes of the stated quality control provisions.

24. Nevertheless, the Task Force believes that the firm and the auditor need to be aware of the difference in definitions, in relation to complying with relevant ethical requirements. Accordingly, the Task Force also recommends that additional application material be provided in proposed ISA 220 (Redrafted) and ISQC 1 (Redrafted) that draws attention to the definition of “firm” in the IFAC Code.

See paragraphs 9(e) and A5 of ISA 220 (Redrafted) in Agenda Item 10-B.

See paragraphs 12(g) and A10 of ISQC 1 (Redrafted) in Agenda Item 10-E.

B.2 RESPONSIBILITIES IN ISA 220

25. At its June meeting, the IAASB noted a comment by a respondent that ED-ISA 220 is in some instances not clear about who is responsible for performing certain specified procedures.

Task Force Recommendations

26. The Task Force agrees that the clarity of the ISA would be enhanced if in all relevant cases the requirements make clear the responsible person(s). The Task Force has therefore redrafted certain paragraphs for this purposes, identifying:

- The engagement quality control reviewer as the person responsible for performing the requirements set out in paragraphs 22-23 of Agenda Item 10-B; and
- The engagement partner as the person responsible for setting review responsibilities at the engagement level.

See paragraphs 18, 22-23 and A17 of ISA 220 (Redrafted) in Agenda Item 10-B

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5 The IFAC Code defines the firm as “(i) A sole practitioner, partnership or corporation of professional accountants; (ii) An entity that controls such parties through ownership, management or other means; and (iii) An entity controlled by such parties through ownership, management, or other means.
B.3 Engagement Team Members with Expertise in a Specialized Area of Accounting or Auditing

27. The ISA 620 Task Force has recommended that proposed ISA 220 (Redrafted) include additional guidance addressing situations where the engagement team includes a member with expertise in a specialized area of accounting or auditing. The Task Force believes this additional guidance to be useful and appropriate.

See paragraph A16 of ISA 220 (Redrafted) in Agenda Item 10-B.

SECTION C – Issues Unique to ISQC 1 Not Covered in Sections A and B

C.1 Definitions

28. At the June IAASB meeting, it was suggested that all applicable definitions in the Glossary of Terms should be added to ISQC 1 (Redrafted).

Task Force Recommendations

29. The Task Force is of the view that ISQC 1 (Redrafted) should contain only those definitions that are essential to an understanding of its requirements. The Task Force believes that all such definitions have been included, with one exception: the term “Date of Report.” The ISAs include a definition for this term in the context of an audit, but proposed ISQC 1 (Redrafted) does not. Accordingly, the Task Force proposes to introduce a definition of this term, applicable generally to any engagement falling within the scope of ISQC 1 (Redrafted).

See paragraph 12(a) of ISQC 1 (Redrafted) in Agenda Item 10-E.

C.2 Expressing Requirements as Policies and Procedures

30. At its June meeting, the IAASB noted a concern raised by a respondent pertaining to the obligation of the firm to comply with the requirements of ISQC 1 (Redrafted) and whether that obligation is appropriate in relation to some of the specific procedures required under the standard. It was noted that a firm’s quality control system is a dynamic one of self-monitoring and self-correction. Compliance within such a system is therefore different from compliance within the context of auditing standards; in a quality control system, there are likely to be inadvertent breaches or deficiencies, or policies and procedures that need to be strengthened, though compensating action can be taken to address a particular deficiency and mitigate its effect, enabling the firm to meet the objective of the firm’s system of quality control. Accordingly, whilst it is possible to say that a firm has policies and procedures designed to comply with ISQC 1 (Redrafted), it may not be possible to assert that the firm has performed all the procedures as set out in the requirements.

Task Force Recommendations

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6 ISA 560 (Redrafted) defines the term “Date of the Auditor’s Report” as “The date the auditor dates the report on the financial statements in accordance with ISA 700.”
31. The Task Force agrees in principle with the point raised. In reviewing the proposed ISQC 1 (Redrafted) with this perspective in mind, the Task Force has identified several paragraphs that call for the firm to perform specific procedures which could better be expressed in terms of required policies and procedures. The Task Force proposes to amend those paragraphs accordingly (see noted paragraphs in the text box below).

32. The Task Force believes, however, that there are certain specific procedures which are required of the firm, and that it would not be appropriate to be expressed them in terms of policies and procedures. The Task Force has therefore not redrafted the following: paragraphs 13-15, 24, 30, 48-51, 53 and 56.

C.3 MONITORING VERSUS COMMUNICATION OF RESULTS

33. Paragraph 48 of the proposed ISQC 1 (Redrafted) in Agenda Item 10-E addresses the firm’s policies and procedures for inspection of a selection of completed engagements on a cyclical basis. Paragraph 53 addresses the firm’s policies and procedures for communication of the results of the firm’s monitoring process at least annually. The IAASB Task Force has been advised that there is some confusion as to whether complying with the requirement in paragraph 53 means that the requirement in paragraph 48 is to be performed annually.

Task Force Recommendations

34. The Task Force believes that the intent of the extant ISQC 1 is for an inspection of a selection of files for each engagement partner on a cyclical basis. Accordingly, the Task Force proposes to amend paragraph 48(a) to make this clear.

C.4 PUBLIC SECTOR CONSIDERATIONS RELATING TO INDEPENDENCE

35. Paragraph A11 of ED-ISQC 1 (paragraph A15 of the Task Force’s June version, unchanged from the ED) contains the following guidance specific to public sector audit organization:

“The independence of public sector auditors may be protected by statutory measures, with the consequence that certain of the threats to independence of the nature envisaged by the material in paragraphs 21-25 and A12-A14 are unlikely to occur. However, threats such as self-review, familiarity and intimidation may still exist regardless of any statutory measures designed to protect independence. Public sector audit organizations consider how to appropriately address any such identified threats.”

36. Based on discussion with the IESBA, the Task Force proposes that this paragraph be deleted for several reasons. First, it could be seen as interpretation of the IFAC Code, which is not appropriate in an IAASB document. Secondly, the Task Force is uncertain

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7 The first sentence was drawn from paragraph 4 of the ‘Public Sector Perspective’ in extant ISQC 1. The second was added during development of ED-ISQC 1 to modify and explain further the meaning of the first sentence.
whether the first sentence is correct, and whether singling out certain, but not all, threats in the second sentence is appropriate. Finally, it is not clear what guidance it actually being provided.

**SECTION D – OTHER DRAFTING CHANGES**

37. Paragraphs 18-21 of the Task Force’s June version of ISA 220 (Redrafted) deal with EQCR. The Task Force notes that there is some repetition among these paragraphs, and believes that they could be made clearer by combining related elements, eliminating unnecessary duplication, and using lists for the various points. The same considerations apply to paragraphs 36-39 of the Task Force’s June version of ISQC 1 (Redrafted). The Task Force believes that the changes it proposes do not represent any change in substance.

See paragraphs 22, 23 and A28 of ISA 220 (Redrafted) in Agenda Item 10-B.

See paragraphs 37, 38 and A44 of ISQC 1 (Redrafted) in Agenda Item 10-E.

**SECTION E – RE-EXPOSURE CONSIDERATION**

38. Agenda Items 10-D and 10-G present the marked versions of the revised drafts of ED-ISA 220 and ED-ISQC 1 from the exposure drafts, respectively.

39. It is the Task Force’s view that the changes made from the exposure drafts reflect responses to comments received or the updating of material for relevant changes in other ISAs and the IFAC Code. The Task Force does not believe they introduce new principles or changes of substance. Accordingly, the Task Force is of the view that re-exposure is not necessary.8

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8 IAASB Working Procedures regarding re-exposure state: “Situations that constitute potential grounds for a decision to re-expose may include, for example: substantial change to a proposal arising from matters not aired in the exposure draft such that commentators have not had an opportunity to make their views known to the IAASB before it reaches a final conclusion; substantial change arising from matters not previously deliberated by the IAASB; or substantial change to the substance of an International Standard or Practice Statement.”