

QUALITY CONTROL: ENGAGEMENT QUALITY CONTROL REVIEW – ISSUES AND WORKING GROUP VIEWS

Objective of the Agenda Item

The objective of this Agenda Item is to obtain the CAG Representatives and Observers' input on certain quality control issues in relation to aspects of engagement quality control reviews (EQC reviews). The input from the CAG Representatives and Observers on these matters will help inform the development of the project proposal for presentation to the IAASB at its December 2016 meeting, and will assist the Quality Control Working Group (WG) in moving forward on all matters relating to EQC reviews.

Introduction

1. A high-level summary of the responses to the IAASB's Invitation to Comment (ITC), *Enhancing Audit Quality in the Public Interest: A Focus on Professional Skepticism, Quality Control and Group Audits*, as well as the proposed way forward on the various projects, including professional skepticism and group audits, is set out in **Agenda Item G.1**. That paper sets out the interactions between the projects on quality control and group audits, and the Enhancements Group's views on possible actions for moving forward. This includes the prioritization of the development of a quality management approach (QMA) for quality control at the firm level and relevant principles for quality management at the engagement level (see paragraph 31 of **Agenda Item G.1**), as well as addressing the 'crossover issues' (see paragraph 62 of **Agenda Item G.1**). The possible options for a way forward in **Agenda Item G.1** in relation to quality control are those of the Enhancements Group and do not necessarily reflect the views of the WG.
2. **Agenda Item G.1** sets out a high-level summary of the responses to the questions relating to quality control in the ITC. As is explained in that agenda item, there is support for moving forward to develop a QMA at the firm level and relevant principles for quality management at the engagement level. As a QMA is being developed, directional aspects of some of the requirements in ISQC 1¹ (such as EQC reviews and human resources and engagement partner competency) need to be determined, and will therefore be discussed as discrete aspects of the quality control project, with the intention that they will be absorbed into the larger quality control project as a QMA is developed (i.e., once drafting commences the requirements and guidance will be developed as part of the revision to ISQC 1).
3. The WG recognizes that EQC reviews (including consideration of when they should be applied) are an integral part of a firm's system of quality control and consequently would also be an integral part of a QMA. For this reason, the WG is aware that EQC reviews cannot be considered in isolation from the other parts of a QMA, including, for example, other forms of reviews and other preventive controls implemented by the firm. The WG is therefore working on EQC reviews in cognizance of the work on the QMA as a whole and other parts of that approach may have an impact on the issues being

¹ International Standard on Quality Control (ISQC) 1, *Quality Control for Accounting firms that Perform Audits and Reviews of Financial Statements and Other Assurance and Related Service Engagements*

addressed. Further information regarding how the discrete issues will be addressed by the WG and integrated into a QMA is set out in paragraph 91 of **Agenda Item G.1**.

4. This paper presents the WG's discussions and views on aspects of EQC reviews for consideration by the CAG. The CAG Representatives and Observers' views on these matters will assist the WG with developing its project proposal on quality control for presentation to the IAASB at its December 2016 meeting. In revising ISQC 1 using a QMA, the WG will also continue to prioritize monitoring and remediation issues and explore how to further strengthen the standard in respect of these matters.
5. Further information about the respondents and a list of respondents to the ITC can be found in Appendix 1 of **Agenda Item G.1**.

Engagement Quality Control Reviews

6. In considering how audit quality could be improved through strengthening the firm's systems of quality control, in the ITC the IAASB proposed the following with respect to EQC reviews:
 - Extending the requirement for an EQC review beyond audits of listed entities. **(Part A)**
 - Addressing the roles and responsibilities of EQC reviewer, including the nature and extent of review. **(Part B)**
 - Improving the transparency about whether an EQC review has been performed. **(Part C)**
 - Enhancing the documentation requirements of an EQC review.
 - Introducing new requirements or application material addressing the selection of the EQC reviewer. **(Part D)**
 - Placing the EQC review into a separate standard. **(Part E)**
7. An analysis of the feedback from respondents and the WG's preliminary views for further CAG consideration in response to this feedback is set out below. However, this paper does not include respondents' feedback to enhancing the documentation requirements of an EQC review, since the WG is of the view that deliberations on this topic depend on the outcome of other discrete issues. Accordingly, the WG will further explore the documentation of the EQC review in due course.
8. The WG recognizes that establishing the objective of the EQC review, including the roles and responsibilities of EQC reviewers, as explained in Part B of this paper, is fundamental to the remaining considerations regarding the matters (other than those in Part B), for example, the objective of the EQC review and the roles and responsibilities of the EQC reviewer impact whether there should be further extension of the requirement for an EQC review beyond audits of listed entities. However, a large number of respondents provided their views regarding whether the requirement for an EQC review should be extended beyond listed entities (Part A), with large variances in these views, and accordingly this paper discusses this matter first.

A. Extend Requirement for an EQC Review Beyond Audits of Listed Entities

Background

9. In the ITC, the IAASB recognized that there are concerns regarding the appropriateness of the criteria established by firms to determine which engagements are subject to an EQC review and that

insufficient focus is being placed on entities of particular public interest² that are not listed entities. The IAASB expressed mixed views regarding possible actions in addressing these concerns. Accordingly, the ITC set out a variety of possible options representing the various views on how this could be addressed, and sought the views of respondents as to whether the requirement for an EQC review should be strengthened, and if so, how this could be best achieved.

Feedback from Respondents³

10. Two members of the Monitoring Group⁴ (MG) responded to this question. One respondent⁵ supported the extension of the requirements for an EQC review to entities that have a large number and wide range of stakeholders (such as insurance companies and pension funds). The other respondent⁶ was supportive of elevating the application material in paragraph A41 of ISQC 1 to the requirements that relates to the criteria for determining which engagements, other than audits of financial statements of listed entities, are to be subject to an engagement quality control review. In addition, separate to the ITC, a letter was sent to the IAASB in March 2013 by another member of the MG,⁷ indicating that all banks should be subject to an EQC review because of the contribution of the EQC review to ensuring the consistency of the quality of audits for these types of entities.
11. Other regulators and audit oversight authorities expressed strong support to extend the requirements for an EQC review beyond audits of listed entities, with mixed views as to how this should be implemented:
 - Support for extending the requirements to entities of particular public interest,⁸ or public interest entities (PIEs)^{9,10} due to the importance and value placed on the EQC review and the role of the EQC reviewer by stakeholders, particularly investors, and because an EQC review is particularly important for audits which require significant judgment. These respondents also highlighted this being an approach consistent with the European Union (EU), where the

² The term “entities of particular public interest” is used here rather than PIEs because PIEs are defined differently in different jurisdictions and by the International Ethics Standards Board (IESBA) *Code of Ethics for Professional Accountants* (Code) for independence purposes.

³ Feedback from respondents generally presents a summary of where respondents had answered a specific question. However, not all respondents answered every question and therefore the summary is only representative of those that did respond.

⁴ The MG comprises the Basel Committee on Banking Supervision (BCBS), the European Commission (EC), the Financial Stability Board (FSB), the International Association of Insurance Supervisors (IAIS), the International Forum of Independent Audit Regulators (IFIAR), the International Organization of Securities Commissions (IOSCO), and the World Bank. BCBS, IFIAR, IAIS and IOSCO responded to the ITC.

⁵ MG: IAIS

⁶ MG: IOSCO

⁷ MG: BCBS

⁸ *Other Regulators and Audit Oversight Authorities*: UKFRC

⁹ A PIE, in this context, would typically include entities falling within the definition of PIE under the IESBA Code. Accordingly, this would typically include listed entities and those defined by local legislation or regulation as PIEs. It is recognized that some jurisdictions have already defined what this means whereas others have not. Therefore in using PIE hereafter it is recognized that some jurisdictions would still need to define what they would consider a PIE if the IAASB were to use that terminology.

¹⁰ *Other Regulators and Audit Oversight Authorities*: EBA

requirement for an EQC review has become a formal and legal obligation for the audit of every public interest entity.¹¹

- Support¹² for a combined approach, i.e., extension for an EQC review to PIEs and incorporating requirements for firms to adopt a risk-based approach to identifying other engagements that should be subject to an EQC review that includes requirements addressing the criteria for selection of engagements.

12. Respondents representing other stakeholder groups also had mixed views regarding this proposal as follows:

- a) Support¹³ to extend the requirements to PIEs, to ensure consistent application in practice, to address the reputational risk of the firm should an audit failure occur at a PIE and to achieve consistency with the IESBA Code regarding more onerous requirements in respect of PIEs.
- b) Support¹⁴ to extend requirements for a firm to establish a risk-based approach to identifying audits of entities other than listed entities that should be subject to an EQC review, together with criteria that indicate which engagements should be subject to an EQC review, supported by enhanced application material. This includes elevating the application material in paragraph A41 of extant ISQC 1 to requirements, which addresses the criteria for determining which engagements should be subject to EQC reviews.
- c) Support¹⁵ for criteria regarding which engagements should be subject to an EQC review that can be consistently applied in various jurisdictions.
- d) Support¹⁶ for a combined approach, i.e., extension for an EQC review to public interest audits and incorporating requirements for firms to adopt a risk-based approach to identifying other engagements that should be subject to an EQC review.
- e) Support¹⁷ for enhancing the application material to support consistent interpretation and application of which engagements should be subject to an EQC review, and to provide clarity on factors that may influence the determination of the necessity for an EQC review.
- f) No support¹⁸ to extend the requirements beyond listed entities to PIEs (or similar), with most of these respondents suggesting that this should be a jurisdictional determination and that the

¹¹ The definition of a public interest entity in the EU Directive 2006/43/EC, was amended by [Directive 2014/56/EU](#).

¹² *Other Regulators and Audit Oversight Authorities*: IRBA

¹³ *NSS*: NBA; *Accounting Firms*: DTT, KPMG; *Member Bodies and Other Professional Organizations*: APESB, ICPAK, WPK; *Individuals and Others*: DAHughes

¹⁴ *NSS*: JICPA, MAASB; *Accounting Firms*: EYG; *Member Bodies and Other Professional Organizations*: AICPA, CPAA, FEE, IRE-IBR, ICPAK, SAICA

¹⁵ *Public Sector Organizations*: AGC, INTOSAI; *Accounting Firms*: BDO; *Member Bodies and Other Professional Organizations*: CPAA

¹⁶ *Accounting Firms*: CHI; *Public Sector Organizations*: AGSA

¹⁷ *NSS*: CAASB, IDW; *Accounting Firms*: PWC, RSM; *Member Bodies and Other Professional Organizations*: ICAEW,

¹⁸ *NSS*: AUASB, CNCC-CSOEC, NZAuASB; *Accounting Firms*: GTI; *Member Bodies and Other Professional Organizations*: CAANZ, EFAA, ICAZ, KICPA, SMPC; *Individuals and Others*: SDeViney

existing requirements in paragraph 35 of ISQC 1 are appropriate. Furthermore, respondents¹⁹ highlighted the difficulty in defining a “PIE” at an international level or determining another definition and the fact that not all PIEs are subject to the same level of risk. In addition, one respondent²⁰ highlighted that other measures may exist at a jurisdictional level instead of EQC reviews, such as joint audits and accordingly more mandatory requirements would ignore other quality control mechanisms.

13. From a small and medium practice (SMP) perspective, national standard setters (NSS) and member bodies representing SMPs²¹ did not support the extension of the requirements for an EQC review beyond listed entities, since in relation to SMPs, there are many audit engagements of entities that could qualify as PIEs, but which are small entities and not risky in nature. Respondents were therefore of the view that such a requirement would be overly burdensome and not contributive to the enhancement of audit quality. A NSS²² also commented that the current approach in ISQC 1 allows flexibility within the firm structure for decisions to be made on an engagement by engagement basis as to whether an EQC review should be performed.
14. Accounting firms and member bodies²³ also noted the EQC review considerations in the context of a QMA, i.e., including risk factors for consideration in a firm’s quality risk assessment process that forms the basis for development of risk-responsive EQC review policies and procedures. One accounting firm²⁴ highlighted the need to also incorporate in the application material the determination of which engagements other than audits of financial statements are subject to an EQC review.
15. Respondents across a few stakeholder groups²⁵ also had the view that a broader approach should be taken to EQC reviews, i.e., addressing other forms of quality control and review, such as other types of reviews, or other mechanisms to address quality, such as joint audits.

WG Views and Matters for Further CAG Consideration

16. In discussing the responses to the ITC and a recommended action to pursue, the WG agreed that there was overall support for further consideration of strengthening the requirements for entities that should be subject to an EQC review. However, as noted above respondents had varying views about how this could be best achieved.
17. In general, respondents did not extensively support a more prescriptive approach to extending the requirements for an EQC review to PIEs or entities of particular public interest, notwithstanding that there were respondents, including two members of the MG, which sought such prescription. In considering the responses and how to address respondents’ broad views, the WG explored the following possible approaches:

¹⁹ *Member Bodies and Other Professional Organizations:* AICPA, EFAA

²⁰ *NSS:* CNCC-CSOEC

²¹ *NSS:* CAASB; *Member Bodies and Other Professional Organizations:* ACCA, EFAA, SMPC

²² *NSS:* AUASB

²³ *Accounting Firms:* EYG, PWC; *Member Bodies and Other Professional Organizations:* IRE-IBR

²⁴ *Accounting Firms:* PWC

²⁵ *Other Regulators and Audit Oversight Authorities:* EAIG; *NSS:* IDW; *Accounting Firms:* GTI; *Public Sector Organizations:* AGC, GAO, INTOSAI; *Member Bodies and Other Professional Organizations:* ICAEW; *Individuals and Others:* SDeViney

- a) Incorporating a prescriptive requirement for an EQC review for audits of entities of particular public interest other than listed entities, through either:
 - Extending the requirement beyond listed entities to PIEs;
 - Extending the requirement beyond listed entities to entities of particular public interest, that would be defined in ISQC 1 for the purposes of EQC reviews; or
 - Extending the requirement to certain specified entities, such as a bank or insurance company.²⁶
 - b) Including a more robust requirement²⁷ regarding the firm's policies and procedures to identify engagements that should be subject to EQC reviews, which are founded on the principle of a risk-based approach and identify robust criteria for firms to take into consideration that should result in entities or engagements of particular public interest being selected.
18. The WG agreed that there was support to strengthen ISQC 1 to include a more robust requirement, with related application material for the firm's consideration of which entities should be subject to EQC review, and agrees that this should be further explored (i.e., paragraph 17(b) above). However, the WG continues to have mixed views regarding whether an EQC review should be required for audits of entities of particular public interest, and if so, how this should be defined in ISQC 1 (i.e., paragraph 17(a) above). These points of view are further explained below.

Requirements for the firm's consideration of which entities should be subject to EQC review

19. Recognizing the general support from respondents to explore a QMA, the WG is of the view that the requirements regarding the firm's policies and procedures to identify engagements that should be subject to EQC review would need to be consistent with a risk-based approach, i.e., the firm would need to establish criteria that identify engagements that pose a risk to the firm's quality objectives.
20. Building on the principle of requirements that adopt a risk-based approach, the WG is of the view that such requirements need to be supported by robust criteria in ISQC 1 for the firm to consider in determining which engagements should be subject to an EQC review. Robust criteria are important for ensuring consistent application across firms in practice. However, the WG is of the view that the criteria set out in paragraph A41 of extant ISQC 1 require strengthening (refer paragraphs 29–31 below for further exploration of the possible criteria).
21. Consistent with the approach in paragraph 5 of ISA 701,²⁸ the WG agrees that the requirements for the firm's consideration of which entities should be subject to an EQC review should also address circumstances when the auditor is required by law or regulation to perform an EQC review. For example, entities may be characterized in law or regulation as public interest entities and may be

²⁶ This option could include specified types of entities, or it could encompass a description that would capture the intent of the requirement, but be less definitive, for example, a deposit-taking institution.

²⁷ Currently, paragraph 35(b) of ISQC 1 requires the firm to "set out criteria which all other audits and reviews of historical financial information [other than listed entities] and related services engagements shall be evaluated to determine whether an engagement quality control review shall be performed...".

²⁸ Paragraph 5 of ISA 701, *Communicating Key Audit Matters in the Independent Auditor's Report*, states "This ISA applies to audits of complete sets of general purpose financial statements of listed entities and circumstances when the auditor otherwise decides to communicate key audit matters in the auditor's report. This ISA also applies when the auditor is required by law or regulation to communicate key audit matters in the auditor's report."

required to be subject to an EQC review (e.g., the requirement in the EU that all audits of PIEs must be subject to an EQC review).

22. Some members of the WG are of the view that the enhanced criteria could be sufficiently robust that it would drive the firm to require an EQC review for audits that are in the public interest, without necessitating an explicit requirement for an EQC review of a PIE or specified types of entities. Furthermore, a risk-based approach supported by robust criteria would be responsive to stakeholders' views as:
- It addresses the concerns of stakeholders that an EQC review is necessary in circumstances where it is in the interests of the public.
 - It is consistent with the principles of a QMA.
 - It supports different environments, i.e., circumstances across firms, jurisdictions and engagements vary and entities and engagements that should be subject to an EQC review would therefore also vary.
 - It allows for a flexible response to quality risk, i.e., an EQC review might not necessarily be the best response to quality control risk in all circumstances.
23. However, as indicated above in paragraph 18, other members of the WG are of the view that a more prescriptive requirement is necessary, as relying on firms to identify engagements that should be subject to EQC reviews poses the risk that firms do not apply this consistently or appropriately, resulting in engagements that should be subject to EQC reviews not being selected (this is discussed further below). Another member of the working group also noted that in considering when an EQC review is required, other courses of action, if appropriate, to address the risk should also be identified. This will be further considered by the WG as the QMA is developed, and in conjunction with other forms of review in the context of monitoring and remediation.
24. If it is determined that prescriptive requirements are not appropriate, a possible further action that could be introduced to help alleviate the concern that entities that should have an EQC review would not be selected, could be to include an explicit requirement in ISA 220²⁹ as part of the principles for quality management at the engagement level, for the engagement partner to consider whether the engagement should be subject to an EQC review. This would create an additional line of defense in ensuring that the quality objectives are met. However, the appropriateness of such a requirement would depend on the objective of the EQC review, as discussed in Part B below. Furthermore, the appointment of the EQC reviewer in such a case would still be through the firm's usual processes and not by the engagement partner themselves.

Incorporating a prescriptive requirement for an EQC review for audits of entities of particular public interest

25. As indicated in paragraph 18 above, some members of the WG are of the view that a more prescriptive requirement is necessary to ensure consistent and appropriate selection of engagements that should be subject to EQC reviews. The WG explored possible ways in which this could be specified in the standard that would be appropriate across many jurisdictions, for example, PIEs, entities of particular public interest or certain other specified entities (e.g., banks or entities

²⁹ ISA 220, *Quality Control for an Audit of Financial Statements*

undertaking insurance activities). Although the majority of respondents commenting on this aspect did not indicate support for an extended requirement that is prescriptive, there were respondents that had the view that this was the most appropriate action (including two MG members). In its deliberations, the WG identified many benefits and challenges of such an approach, including the following:

Benefits

- It is viewed to be more responsive to the public interest, increasing confidence in the audit.
- It would ensure consistent application of the requirements in practice.
- It is more consistent with the approach adopted in certain jurisdictions, for example, the EU where a requirement exists for an EQC review on all audits of PIEs as defined in the EU legislation.

Challenges

- It is difficult to establish an appropriate basis, or definition, that would be suitable for all jurisdictions (i.e., PIEs, PIEs as defined by ISQC 1 for purposes of EQC review, or certain specified entities).³⁰
- It is inconsistent with the approaches adopted in other International Standards on Auditing (ISAs), such as ISA 701 and ISA 260 (Revised),³¹ which contain requirements that are more prescriptive only for listed entities.
- Certain entities could be scoped in that are not a risk to quality, or an exposure to the public.
- It is not responsive to the concerns of SMPs, many of whom may inadvertently be scoped in.
- It could be viewed as contrary to the risk-based approach and principles of a QMA.
- An EQC review may not be the most effective and efficient response to the risk in all circumstances, i.e., another type of control to address quality may be more appropriate.

26. The WG considered the IAASB's deliberations on the approach in ISA 701 regarding those entities required to present key audit matters, and whether this could be considered analogous to the approach for requiring an EQC review.

³⁰ Establishing a definition in ISQC 1 would require agreement on a definition that would be suitable in all jurisdictions using the ISAs. The IESBA definition depends on local legislation or regulation to define PIEs, which is inconsistent across jurisdictions and there are some jurisdictions who have not established a definition of PIE. Furthermore, there are views that the IESBA definition (and those of the jurisdictions who have defined PIEs in accordance with the IESBA definition) is designed for a specific purpose that would not be appropriate in the context of EQC reviews.

³¹ ISA 260 (Revised), *Communication with Those Charged with Governance*

27. In response to the Exposure Draft, *Reporting on Audited Financial Statements: Proposed New and Revised International Standards on Auditing*, respondents, including two members of the MG, were of the view that ISA 701 should apply to PIEs (specifically in order to scope in banks and insurance companies, regardless of whether they were listed entities). In order to respond to feedback from these respondents about the likely interest and perceived importance of key audit matters from the perspective of users of financial statements of PIEs, the IAASB included additional application material in paragraphs A40 and A41 of ISA 700 (Revised)³² to further explain circumstances in which auditors may consider it necessary or may be required to apply ISA 701:
- A40. Law or regulation may require communication of key audit matters for audits of entities other than listed entities, for example, entities characterized in such law or regulation as public interest entities.
- A41. The auditor may also decide to communicate key audit matters for other entities, including those that may be of significant public interest, for example, because they have a large number and wide range of stakeholders and considering the nature and size of the business. Examples of such entities may include financial institutions (such as banks, insurance companies, and pension funds), and other entities such as charities.
28. As highlighted previously, the WG agrees that a risk-based approach supported by robust criteria would be an appropriate mechanism to strengthen ISQC 1. However, as noted the WG has mixed views regarding whether a risk-based approach is sufficient to address concerns regarding consistent and appropriate application in practice that audits that are in the public interest are subject to an EQC review.

Strengthening the requirement for the firm's consideration of which entities should be subject to EQC review

29. The WG explored how the existing requirements of ISQC 1 could be improved to ensure that there is better consistency in practice in terms of which engagements are subject to an EQC review, and to ensure that engagements that pose a high risk to the quality objectives or that have a particular public interest are included. The WG is of the view that the requirements need to be strengthened by requiring firms to establish risk-based criteria that would identify engagements that should be subject to an EQC review, together with robust minimum criteria specified in ISQC 1 (in essence presumed risks).
30. While paragraph A41 of extant ISQC 1 identifies certain criteria, the WG is of the view that this needs to be strengthened (see above). Accordingly, the WG explored the criteria used in other standards and codes that try to achieve similar principles, including:
- Paragraph A41 of ISA 700 (Revised) that was introduced to highlight scenarios where the communication of key audit matters may be appropriate (see paragraph 27 above).
 - Section 290.26 of the IESBA Code, which indicates that firms and member bodies are encouraged to determine whether to treat additional entities, or certain categories of entities, as public interest entities under the IESBA Code.

³² ISA 700 (Revised), *Forming an Opinion and Reporting on Financial Statements*

31. In light of the above, the WG envisages that the risk-based criteria could include the following (this would be dependent on whether prescriptive requirements are incorporated into ISQC 1 to require an EQC review for PIEs or specified entities):
- a) Entities with a large number and wide range of stakeholders, to be established by the firm. Examples of such entities may include those operating in the public sector.
 - b) Entities with certain characteristics in terms of their nature and size, established by the firm in the context of their jurisdiction and the industries. Examples of such entities may include a financial institution (such as a bank, insurance company and pension fund), and other entities such as charities. Some members of the WG believe that further specification of the types of banks, insurance companies and pension funds may be needed in this respect.
 - c) Engagements where there are unusual circumstances or risks, to be defined by the firm. Examples of such engagements may include circumstances where the firm has reissued the auditor's report in a prior period, or there is a material restatement of the comparative information.
 - d) The nature of the engagement, by its nature, includes a matter that is of particular public interest. For example, an assurance engagement on a greenhouse gas statement (that includes information on extensive or controversial environmental matters) may be of particular public interest.

Matters for CAG Consideration

1. With regard to extending the EQC review to entities beyond listed entities, CAG Representatives and Observers are asked:
 - (a) Whether they agree with the WG's views that there is support for strengthening the requirements for an EQC review beyond listed entities?
 - (b) For their views, in light of the responses to the ITC and the matters set out above, for extending the EQC review to entities that are specified in the standard (such as PIE's or specified entities such as banks or entities undertaking insurance activities). If CAG Representatives and Observers agree with extending to entities that are specified in the standard:
 - (i) Should this be PIE's, for example the IESBA definition or another definition determined for the purposes of ISQC 1, specified entities such as banks or insurance entities, or both?
 - (ii) If this is extended to specific types of entities such as banks and insurance entities, are there any other types of entities that should be considered?
 - (c) Irrespective of whether a prescriptive approach is considered appropriate (refer question 1(b) above), do the CAG Representatives and Observers agree with the WG's proposal to strengthen the existing requirements for the firm's consideration of engagements that should be subject to an EQC review, through a risk-based approach supported by robust criteria?
2. CAG Representatives and Observers are asked to share their views regarding the possible minimum criteria identified in paragraph 31, and whether any further criteria should be considered.

B. Roles and Responsibilities of EQC Reviewer, Including Nature and Extent of Review

Background

32. In the ITC, the IAASB acknowledged concerns regarding the timing of the performance of the EQC review, specifically with respect to when the EQC reviewer becomes involved and the time allocated to the EQC reviewer for the performance of the EQC review. Furthermore, the ITC identified the depth and the focus of the review as concerns of stakeholders, specifically highlighting a perception that, in some cases, the EQC reviewer paid insufficient attention to the assessment of and response to areas of significant risk or significant judgments made by the engagement partner and the engagement team, including how, and in which areas of the audit, the engagement team utilized audit delivery models.
33. Accordingly, the ITC suggested that a possible action is to address the role of the EQC reviewer in relation to the engagement partner by strengthening the requirements and application material in ISA 220 through further specifying the nature and extent of matters to be considered by the EQC reviewer. It was suggested that this could include, for example, emphasizing:
- The importance of the EQC reviewer's responsibilities for assessing the judgments made by the engagement partner and the engagement team in determining the areas of significant risk and procedures performed in responding to those significant risk areas.
 - The need for involvement in the review of components in a group audit situation as appropriate.
34. The ITC also explored adding application material to ISA 220 for the use of subject-matter experts or other qualified individuals, separate from subject-matter experts that assisted the engagement team, to assist an EQC reviewer where appropriate.

Feedback from Respondents

35. A member of the MG³³ believed that the objective of EQC review needs to be more clearly defined, since this would help drive improved behavior by EQC reviewers and audit firms in performing reviews and establishing policies and procedures of EQC reviews. Furthermore, this respondent encouraged the IAASB to clarify and highlight the principle of professional skepticism in the performance of an EQC review and recommended that this be reflected in requirements for the EQC reviewer to review and challenge the audit work performed in respect of the judgmental and higher risk areas, thereby clearly addressing the significant decisions made by the engagement partner. Similarly, another member of the MG³⁴ believed that suitable quality control arrangements over areas that require the exercise of a high degree of judgment, such as accounting estimates, are required.
36. Other respondents across other stakeholder groups,³⁵ including other regulators and audit oversight authorities,³⁶ that responded to this aspect of EQC reviews expressed overall support for clarifying and addressing the roles and responsibilities of the EQC reviewer. However, certain of these

³³ MG: IFIAR

³⁴ MG: BCBS

³⁵ *Investors and Analysts:* CFA; *NSS:* AUASB, CAASB, CNCC-CSOEC, IDW, JICPA, NBA; *Accounting Firms:* GTI, KPMG, PWC; *Member Bodies and Other Professional Organizations:* CAANZ, FEE, ICAP, SAICA, SMPC

³⁶ *Other Regulators and Audit Oversight Authorities:* EBA, IRBA, UKFRC

respondents cautioned that the roles and responsibilities of the EQC reviewer should remain appropriate in relation to those of the engagement partner. One regulator and audit oversight authority³⁷ had the view that the existing requirements and application material addressing the responsibilities of the EQC reviewer are sufficient.

37. Similar to the comment from the member of the MG, a range of respondents³⁸ also had the view that the objective of the EQC review needs to be more clearly described as this is important to establishing the responsibilities of the EQC reviewer and to addressing misunderstandings as to where within the firm's quality management framework an EQC review resides. It was further highlighted that the current definition may no longer be sufficient to address what is expected of an EQC review.³⁹ A regulator and audit oversight authority⁴⁰ indicated that in their view, the purpose of the EQC review is a firm level control, and therefore it should not be left to the engagement team to determine whether or not an EQC is required. Another regulator and audit oversight authority⁴¹ expressed the view that the objective should address the extent and timing of the EQC review, including the depth of the review.
38. There was also broad support from other regulators and audit oversight authorities⁴² and across other stakeholder groups⁴³ to clarify the nature and extent of the EQC review as proposed in the ITC (e.g., significant risks, areas of judgment and the work of components), as well as the timing of the EQC review.⁴⁴ Certain respondents representing NSS, accounting firms and member bodies⁴⁵ indicated a preference for application material in this regard, while others⁴⁶ highlighted a preference for specifying the nature and extent of matters to be considered by the EQC reviewer. One regulator and audit oversight authority⁴⁷ advocated exploring more requirements, for example, timing and the engagement team's response and reactions to matters raised during the review.
39. An accounting firm⁴⁸ highlighted the need to retain a flexible approach through the EQC reviewer adopting a risk-based approach, i.e., understanding the risks driving the audit strategy and then considering the level of interaction and review necessary to evaluate the significant judgments related to these risks (which may necessitate, for example, the involvement of an expert, interactions with

³⁷ Other Regulators and Audit Oversight Authorities: MAOB

³⁸ Other Regulators and Audit Oversight Authorities: CPAB, UKFRC Accounting Firms: PWC; Member Bodies and Other Professional Organizations: ICAP, SAICA

³⁹ Member Bodies and Other Professional Organizations: SAICA

⁴⁰ Other Regulators and Audit Oversight Authorities: UKFRC

⁴¹ Other Regulators and Audit Oversight Authorities: CPAB

⁴² Other Regulators and Audit Oversight Authorities: CPAB, ESMA, UKFRC

⁴³ NSS: AUASB, CAASB, JICPA, MAASB, NZAuASB; Accounting Firms: BDO, CHI, DTT, EYG; Public Sector Organizations: AGSA; Member Bodies and Other Professional Organizations: AICPA, CAANZ, CPAA ICAZ, KICPA, SAICA

⁴⁴ Other Regulators and Audit Oversight Authorities: EBA, ESMA, UKFRC; NSS: AUASB, MAASB, NBA, NZAuASB; Accounting Firms: BDO, RSM; Member Bodies and Other Professional Organizations: AICPA, CAANZ, FEE, IRE-IBR, SAICA

⁴⁵ NSS: NZAuASB; Accounting Firms: BDO; Member Bodies and Other Professional Organizations: AICPA, CAANZ

⁴⁶ Other Regulators and Audit Oversight Authorities: UKFRC; NSS: JICPA; Member Bodies and Other Professional Organizations: SAICA

⁴⁷ Other Regulators and Audit Oversight Authorities: UKFRC

⁴⁸ Accounting Firms: EYG

those charged with governance (TCWG) or reviewing component auditor documentation). A similar point was noted by a member body⁴⁹ that the EQC reviewer should evaluate the risk assessment judgments made by the engagement team and not only focus on the risk response.

40. In addition, respondents across stakeholder groups⁵⁰ noted the EQC reviewer's responsibilities to challenge the application of professional skepticism by the engagement team, or the EQC reviewer's own application of professional skepticism.⁵¹ A NSS⁵² highlighted their preference for these enhancements to be in the form of application material or guidance. It was also highlighted by a regulator and audit oversight authority⁵³ that the EQC reviewer should foster the exercise of professional skepticism from the planning stage of an audit.
41. There was one respondent representing NSS⁵⁴ in favor of the proposed action to emphasize the need for involvement by the EQC reviewer in the review of components in a group audit situation as appropriate. However, an accounting firm⁵⁵ didn't agree with this proposal since the EQC reviewer should instead evaluate key judgments made with regards to engagement scope and the conclusions drawn by the group engagement team on any significant matters that have arisen at components.
42. Respondents from NSS and accounting firms⁵⁶ did not believe it appropriate for the EQC reviewer to be supported by experts, since the role of the EQC reviewer is not to re-perform the engagement and is instead to understand the process followed by the engagement team in understanding and reviewing the work of the specialist/expert and the related conclusions and to hold discussions with the partner and specialist/expert as deemed necessary. However, member bodies⁵⁷ did support this proposal, although it was noted that this would need to be guidance-based so as not to inadvertently create a re-performance of the audit.

WG Views and Matters for Further CAG Consideration

43. Overall, the WG is of the view that stakeholders support actions to address the roles and responsibilities of the EQC reviewer, including the nature and extent of review.

Objective of the EQC review

44. The WG noted respondents' suggestions, including a member of the MG, to first establish the objective of an EQC review, as this was seen to be important to establishing the responsibilities of the EQC reviewer and to addressing misunderstandings as to where within the firm's quality management framework an EQC review resides. The WG noted that paragraph 138 of the ITC

⁴⁹ *Member Bodies and Other Professional Organizations:* SAICA

⁵⁰ *Other Regulators and Audit Oversight Authorities:* CPAB, EBA; *NSS:* NZAuASB; *Accounting Firms:* EYG; *Individuals and Others:* JGrant

⁵¹ *NSS:* NZAuASB; *Accounting Firms:* EYG

⁵² *NSS:* NZAuASB

⁵³ *Other Regulators and Audit Oversight Authorities:* EBA

⁵⁴ *NSS:* JICPA

⁵⁵ *Accounting Firms:* PWC

⁵⁶ *NSS:* JICPA; *Accounting Firms:* DTT, KPMG

⁵⁷ *Member Bodies and Other Professional Organizations:* AICPA, CPAA, KICPA, SAICA

highlighted that a potential area for improvement in ISQC 1 could be to include an objective of the performance of an EQC review, as it was highlighted that the US Public Company Accounting Oversight Board's (PCAOB) equivalent standard, Auditing Standard No. (AS) 7,⁵⁸ includes this.

45. The WG agrees with respondent's views that by articulating an objective, the roles and responsibilities of the EQC reviewer would then become clear, which would then drive the nature and extent of the review. Regardless of whether a separate EQC standard is developed or not, the WG will consider where this objective would be best located within the standard.
46. Respondents to the ITC were supportive of the IAASB further exploring a QMA and a risk-based approach to quality at an engagement level. In light of this, the WG deliberated what the purpose of an EQC review would be and where it would be integrated within the QMA. In particular, the WG considered whether the EQC review is:
- Alternative 1: The firm's response to a quality risk (the engagement partner is responsible for engagement quality at the engagement level; the firm also has a responsibility for engagement quality and the EQC review is one of the firm's controls for safeguarding quality);
 - Alternative 2: A response to quality risk at an engagement level (the engagement partner is responsible for engagement quality at the engagement level and the EQC review is a mechanism for challenging the judgments of the engagement team to help ensure that the report is appropriate in the circumstances); or
 - Alternative 3: A combination of both (a) and (b).

In the view of the WG, the objective of the EQC review would depend on which of the above three options is viewed to be the ultimate purpose. There are different views among the WG as to which of the options above might be appropriate. The WG agreed that further consideration of the most appropriate approach is needed, and each of the alternatives is discussed further below.

47. In analyzing the comments from respondents, the WG recognized a common theme: EQC reviews are falling short of the intended purpose, and improvements are needed that would achieve a more robust outcome. In particular the WG noted concerns from respondents regarding matters such as the timing, whether there is sufficient challenge of the engagement team, the EQC reviewer's responsibility and the authority of the EQC reviewer. Accordingly, some members of the WG are of the view that the objective would need to facilitate an EQC review that is deeper and broader.
48. Consistent with views expressed by respondents, the WG agrees that there needs to be clarity that the EQC reviewer is expected to be involved throughout the process of the engagement, and not merely to perform a "tick-box exercise" at the end of the engagement. Regardless of the purpose of the EQC review as indicated in paragraph 46, the WG is of the view that the timing of the EQC review should be incorporated in the objective so that this expectation is clear, with application material that further enhances this principle.

Alternative 1: The EQC review is the firm's response to a quality risk

49. If it is determined that the EQC review is the firm's response (i.e., a control activity) to a quality risk, the objective of the EQC review would be outcome-based, to fit within the concept of a QMA. An

⁵⁸ AS 7, *Engagement Quality Review*

outcome-based objective is consistent with the current principle of a control objective as explained in the *Glossary of Terms*.⁵⁹

50. The current definition of an EQC review in ISQC 1⁶⁰ implies a process-based objective, because it focuses the EQC reviewer on performing procedures rather than encouraging the EQC reviewer to exercise their judgment in determining how to perform the EQC review to achieve the desired outcome. For example, under the current definition, it focuses the EQC reviewer on performing an objective evaluation of the significant judgments made by the engagement team, which describes a procedure. A process-based objective is disadvantageous because it has a narrow focus, which could be viewed as potentially undermining the quality of the review.
51. An outcome-based objective, rather than a process-based objective, would contribute to addressing the robustness of the EQC review, by focusing on such matters as whether an EQC review should be performed, the selection of the EQC reviewer and the nature, timing and extent of the EQC review.
52. Consistent with current practice, an effective EQC review may result in a variety of responses to achieve the outcome, for example, in response to matters raised by the EQC reviewer, the engagement team may perform a reassessment of the risks, further work in a particular area or reconsider the auditor's report. Overall, the outcome would be to ensure that the firm is not exposed to risks arising from poor quality.
53. The WG explored how to articulate this objective in ISQC 1. In order to focus on an outcome, the objective would need to make reference to achieving quality. The WG recognizes the difficulty in defining quality, and such a definition would also need to be applicable to a variety of engagements. If it is determined that the objective of the EQC review should be a firm's response to quality risk, the WG will further deliberate how to link the objective to achieving quality, without inappropriately broadening the responsibility of the EQC reviewer.

Alternative 2: The EQC review is a response to quality risk at an engagement level

54. Under this alternative, a possible approach to determining the objective is to link the objective to the current objective in paragraph 11 (b) of ISQC 1, which is to "evaluate whether reasonable assurance has been obtained that the report issued by the firm or an engagement partner for a particular engagement is appropriate in the circumstances." This would be output-based because the report (and its appropriateness, which is a central indicator of quality) is the primary output of an engagement.
55. In addition to linking to the output of an engagement, the WG considered whether this objective should build on the current definition of an EQC review, and make reference to evaluating the significant judgments made by the engagement team. However, as set out in paragraph 47, some members of the WG are of the view that the objective would need to facilitate an EQC review that is deeper and broader, and adapting the existing requirements may not achieve this.

⁵⁹ The *Glossary of Terms* published by the IAASB defines a control objective as follows: The aim or purpose of a particular aspect of controls. Control objectives relate to risks that controls seek to mitigate.

⁶⁰ *Engagement quality control review*—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 for audits of financial statements of listed entities and those other engagements, if any, for which the firm has determined an engagement quality control review is required.

56. The WG also considered whether correlating the objective more closely to the objectives set out in paragraph 6 of ISA 220 would be more suitable, for example, the work performed complies with professional standards and applicable legal and regulatory requirements. While this creates a direct link to addressing the risks to quality at an engagement level and addresses concerns regarding the robustness of the EQC review, it could be viewed as being too broad and creating an unreasonable expectation of the role of the EQC reviewer.

Alternative 3: A combination of the firm's response to quality risk and a response to quality risk at an engagement level

57. Under this approach, the objective would be a combination of the above two suggestions.

Roles and responsibilities and nature, timing and extent of review

58. Overall, the WG is of the view that there is support to enhance the requirements and application material addressing the nature, timing and extent of the EQC review.
59. However, as indicated above, the WG is of the view that the objective would determine the roles and responsibilities of the EQC reviewer, which in turn impacts the nature and extent of the review. Accordingly, the WG will further deliberate the roles and responsibilities of the EQC reviewer and the nature, timing and extent of the review once the WG has further clarity on the proposed objective.

Matters for CAG Consideration

3. CAG Representatives and Observers are asked:
- (a) Whether an objective for the EQC review should be determined and included in the standards?
 - (b) If yes to (a) above, whether, in their view, the objective for the EQC review being explored by the WG should be a firm-level objective (alternative 1), an engagement-level objective (alternative 2) or a combination thereof (alternative 3)?
4. With respect to the engagement-level objective, and notwithstanding the CAG Representatives and Observers' views above, the CAG Representatives and Observers are asked to share their views regarding whether the engagement-level objective should focus more specifically on the significant judgments made by the engagement team, or is it appropriate for the objective to be broader than significant judgments?

C. Transparency and Interactions with TCWG

Background

60. The ITC explored the possibility of providing transparency in the auditor's report, for example, by communicating in the auditor's report as to whether the engagement was subject to an EQC review. It was noted that any such communication would need to take into account the fact that users of the auditor's report could inadvertently form a negative view about the quality of an audit that has not been subject to an EQC review, notwithstanding that such an audit may not have met the firm's criteria for selection.

61. The ITC also explored whether it would be appropriate to require the communication to TCWG that the engagement is subject to an EQC review, as well as whether, and in what circumstances, communication between the EQC reviewer and TCWG may be appropriate.

Feedback from Respondents

62. Respondents across all stakeholder groups, including one regulator and audit oversight authority,⁶¹ did not support providing transparency in the auditor's report related to the engagement being subject to EQC review, indicating that this could create the misconception that audits not subject to EQC review are of poorer quality or that those engagements selected were higher risk. It was also noted that the EQC review is merely one element of a greater system of quality control. There was limited support from NSS and member bodies, as well as an investor,⁶² for the communication that the engagement is subject to EQC review to be with TCWG, although others⁶³ did not agree. It was highlighted that communication with TCWG would necessitate explaining why the engagement has been selected, the role of the EQC reviewer and perhaps even the results of the EQC review, which is not appropriate.⁶⁴
63. Respondents across all stakeholder groups⁶⁵ raised concerns with the EQC reviewer interacting with TCWG, noting the fundamental principle of the EQC reviewer's role to be independent from the engagement team and objectively challenge the decisions made without being inappropriately influenced by management or TCWG. An accounting firm⁶⁶ believed that the standards should not include or preclude such a requirement but allow a flexible approach as considered necessary for the circumstances.

WG Views and Matters for Further CAG Consideration

64. The WG identified that there was little support for providing transparency in the auditor's report on whether an EQC review was performed, and limited support for communicating that the engagement was subject to EQC review to TCWG. The WG also noted that overall, respondents were not supportive of introducing requirements or additional application material addressing the EQC reviewer's interaction with TCWG.
65. Accordingly, the WG proposes that no additional requirements or application material are needed to address communication about the EQC review.

⁶¹ *Other Regulators and Audit Oversight Authorities:* IRBA; *NSS:* CAASB, CNCC-CSOEC, IDW, JICPA, MAASB; *Accounting Firms:* EYG, KPMG, PWC; *Public Sector Organizations:* AGC, AGSA, GAO, INTOSAI; *Member Bodies and Other Professional Organizations:* FEE, ICAEW, KICPA, SAICA, WPK

⁶² *Investors and Analysts:* CalSTRS; *NSS:* AUASB, CNCC-CSOEC, IDW; *Member Bodies and Other Professional Organizations:* FEE

⁶³ *Accounting Firms:* EYG; *Member Bodies and Other Professional Organizations:* AICPA, KICPA

⁶⁴ *Accounting Firms:* EYG

⁶⁵ *NSS:* IDW, JICPA; *Accounting Firms:* DTT, KPMG; *Public Sector Organizations:* AGSA; *Member Bodies and Other Professional Organizations:* AICPA, CAANZ, ISCA, KICPA, WPK

⁶⁶ *Accounting Firms:* EYG

Matter for CAG Consideration

5. Do the CAG Representatives and Observers agree with the WG's conclusion that no further actions are necessary to address communication in the auditor's report about the EQC review, or the interactions with TCWG?

D. Selection of the EQC Reviewer

Background

66. In the ITC, the IAASB noted concerns regarding the selection of the EQC reviewer, including the qualifications, experience and objectivity of the individual selected to perform the EQC review, and consideration of the reviewer's own inspection results.
67. The ITC included possible actions for the requirements and application material regarding the selection of the EQC reviewer to be strengthened, for example, by elevating to requirements the application material in ISQC 1 concerning policies and procedures to maintain objectivity of the EQC reviewer. There was also a suggestion to introduce a requirement for the firm to establish a policy that defines the period of time that an individual who had previously been involved in the audit, including in the role of the engagement partner, would not be eligible to fill the role of the EQC reviewer.

Feedback from Respondents

68. Members of the MG⁶⁷ were supportive of more robust requirements addressing the selection of the EQC reviewer, including the integrity, objectivity and independence of the EQC reviewer,⁶⁸ and the technical expertise, experience and authority of the EQC reviewer.⁶⁹ One of these respondents was of the view that enhanced application material to address the seniority of the EQC reviewer to avoid hierarchical mismatches is necessary, and such guidance should not be limited to audits of listed entities.⁷⁰ A member of the MG⁷¹ also believed that paragraph A49 of ISQC 1 regarding maintaining the objectivity of the EQC reviewer and A47 of ISQC 1 related to the sufficient and appropriate technical expertise, experience and authority of the EQC reviewer should be elevated to requirements. Furthermore, it was suggested by another member of the MG⁷² that the selection criteria should consider the results of audit quality assessments, both external and internal.
69. Respondents from other stakeholder groups,⁷³ including a regulator and audit oversight authority,⁷⁴ agreed with the proposed actions to address the selection of the EQC reviewer through enhanced

⁶⁷ MG: IAIS, IOSCO

⁶⁸ MG: IAIS

⁶⁹ MG: IOSCO

⁷⁰ MG: IOSCO

⁷¹ MG: IOSCO

⁷² MG: IFIAR

⁷³ NSS: CAASB, IDW; Accounting Firms: PWC; Member Bodies and Other Professional Organizations: CPAA, FEE, ICAZ, SAICA; Academics: AAA; Individuals and Others: DAHughes

⁷⁴ Other Regulators and Audit Oversight Authorities: UKFRC

requirements and application material, with two member bodies⁷⁵ specifically supporting application material. Respondents⁷⁶ believed that the independence, integrity and objectivity of the EQC reviewer should be addressed. There was also a suggestion that the ability of the EQC reviewer to challenge the engagement team's judgements with confidence should be addressed⁷⁷ as well as the authority of the EQC reviewer.⁷⁸ However, a respondent⁷⁹ highlighted that the role should not be restricted to partners. An academic⁸⁰ highlighted evidence that partners in close geographic proximity, and with expertise in the industry, tend to provide more thorough reviews. Generally, however, it was cautioned that the requirements should not be so onerous that the availability of suitable EQC reviewers is limited or non-existent, especially for SMPs.

70. There were mixed views regarding whether the IAASB should address the cooling-off period (i.e., the time that an individual who had previously been involved in the audit would not be eligible to fill the role of the EQC reviewer) of the EQC reviewer in ISQC 1. MG respondents did not comment specifically on this matter. Various options as to how the matter could be addressed and by whom were raised as follows:

Actions by the IAASB

- A requirement in ISQC 1 for the firm to define the cooling-off period.⁸¹
- Calls, mostly from regulators and other oversight authorities and public sector organizations,⁸² for the IAASB to define a minimum cooling-off period.
- Support from an accounting firm⁸³ for establishing requirements for a cooling-off period, but not mandating a specific period, as mandating a specific period would depend, in part, on the nature and complexity of the engagement, and local laws and regulations.
- Concern from a few stakeholder groups⁸⁴ that the IAASB should not address the cooling-off period. These respondents cited concerns that prescribing the cooling-off period would become too rules-based and that the standards should instead focus on the principle of the EQC reviewer's objectivity.

⁷⁵ *Member Bodies and Other Professional Organizations:* IRE-IBR, ICAEW

⁷⁶ *Other Regulators and Audit Oversight Authorities:* UKFRC; *NSS:* NBA; *Accounting Firms:* DTT, EYG, PWC; *Public Sector Organizations:* AGSA; *Member Bodies and Other Professional Organizations:* ICAZ, ISCA, SAICA

⁷⁷ *Other Regulators and Audit Oversight Authorities:* UKFRC

⁷⁸ *Accounting Firms:* GTI; *Member Bodies and Other Professional Organizations:* CPAA

⁷⁹ *Member Bodies and Other Professional Organizations:* ICAEW

⁸⁰ *Academics:* AAA

⁸¹ *National Standard Setters:* JICPA; *Member Bodies and Other Professional Organizations:* ACCA, FEE, IBRACON, ICAEW, SAICA

⁸² *Regulators and Audit Oversight Bodies:* IRBA, UKFRC; *Accounting Firms:* CHI; *Public Sector Organizations:* AGSA, GAO

⁸³ *Accounting Firms:* BDO

⁸⁴ *Accounting Firms:* EYG, RSM; *Member Bodies and Other Professional Organizations:* AICPA, CPAA; *Individuals and Others:* DAHughes, SDeViney

Actions by the IESBA (Potentially in Coordination with the IAASB)

- While agreeing that the cooling-off period should be addressed, some respondents⁸⁵ were of the view that it is a matter that should be addressed by IESBA. There were also recommendations that the IESBA should address this in coordination with the IAASB.
- Support from an accounting firm⁸⁶ for collaboration between the IAASB and IESBA.
- Support from a member bodies⁸⁷ for both the IAASB and IESBA to address the cooling-off period.
- There were also respondents who did not indicate whether they supported the action or not, but noted that it was a matter for the IESBA.⁸⁸

71. Respondents highlighted the difficulty for SMPs regarding proposals addressing the selection of the EQC reviewer. In particular, NSS and member bodies⁸⁹ noted that SMPs already experience difficulties in identifying an appropriate EQC reviewer and that further restrictions would create problems in practice in finding suitable candidates. It was also noted by an accounting firm⁹⁰ that too much regulation and too many requirements has hampered the ability of SMPs to continue in operation, which has resulted in fewer audit firms being able to provide an audit service.

WG Views and Matters for Further CAG Consideration

Criteria for the eligibility of the EQC reviewer

72. The WG noted that there was a limited response regarding the selection of the EQC reviewer, with members of the MG indicating strong support for this to be addressed and providing suggestions of matters to be considered by the IAASB. Accordingly, the WG has the view that the robustness of the criteria addressing the eligibility of the EQC reviewer in the ISQC standards needs improvement.
73. The WG recognizes that the criteria for the eligibility of the EQC reviewer will need to be considered in light of the objective of the EQC review and the responsibility of the EQC reviewer. Nevertheless, the WG explored some initial thinking, building on the existing requirements in paragraph 39 of extant ISQC 1 and taking into consideration the views of respondents, regarding what the criteria could be. Some initial ideas of the WG regarding the criteria for the eligibility of the EQC reviewer are:
- Including more robust requirements for the firm to establish a process for the selection of the EQC reviewer, to ensure that the EQC reviewer who is selected has the appropriate competencies, integrity and objectivity to perform the review and is independent. This would need to emphasize that the firm's process should ensure that the EQC reviewer is selected by someone unconnected to the engagement team, for example, in respect of audits of listed entities, this requirement could explicitly indicate that the EQC reviewer should not be selected by the engagement partner, and in circumstances where it is not possible for the engagement

⁸⁵ *National Standard Setters:* CAASB, CNCC-CSOEC, NZAuASB; *Accounting Firms:* GTI; *Public Sector Organizations:* AGC, INTOSAI; *Member Bodies and Other Professional Organizations:* IRE-IBR.

⁸⁶ *Accounting Firms:* PWC

⁸⁷ *Member Bodies and Other Professional Organizations:* APESB

⁸⁸ *Member Bodies and Other Professional Organizations:* CAANZ, CPAA, EFAA, ICAZ

⁸⁹ *NSS:* CAASB, IDW; *Member Bodies and Other Professional Organizations:* ACCA, AICPA, FEE, ICAEW, KICPA, SMPC

⁹⁰ *Accounting Firms:* BDO

partner to be excluded from the selection process (e.g., a SMP where there is only one engagement partner) that other mechanisms are in place to safeguard the objectivity of the EQC reviewer from the engagement.

- Requirements for the firm to establish policies and procedures that address the EQC reviewer's authority within the firm, in order to support the EQC reviewer's ability to challenge the judgments made by the engagement team.
- Requirements for the firm to establish policies and procedures addressing the EQC reviewer's necessary level of knowledge and competence, relevant to the EQC review, in the context of the engagement in order to be able to perform the review effectively. The requirements could explicitly require that for audits of listed entities, the EQC reviewer should possess the level of knowledge and competence and professional values, ethics and attitudes, relevant to the EQC review, which is required to serve as the engagement partner on the audit. The application material could further explain that the required knowledge and competencies that are relevant to the EQC review does not need to address all of the knowledge and competencies that are expected of an engagement partner under International Education Standard (IES) 8 (Revised),⁹¹ for example, organizational and interpersonal and communication skills would typically not be relevant to the performance of the EQC review.

74. Application material to support the above requirements would be essential. In relation to the necessary competence of the EQC reviewer, the application material could also discuss that the considerations would usually include considering the results of both external and internal audit quality assessments of the EQC reviewer, in the context of the risk of the engagement, for example, in some circumstances it may not be appropriate for an individual with poor inspection results to perform the role of EQC reviewer if there are greater quality risks associated with the engagement; however in other circumstances the individual may be a suitable candidate.

Cooling-off period

75. The WG agreed that respondents overall supported actions to address the period of time that an individual who had previously been involved in the audit, including in the role of the engagement partner, would not be eligible to fill the role of the EQC reviewer. However, similar to respondents, the WG had mixed views as to how this should be addressed. These views included requirements for a minimum cooling-off period or a range of a period, requirements for the firm to establish a policy addressing a cooling-off period or leaving the matter for IESBA to address.
76. The WG noted the IESBA's project addressing the long association of audit firm personnel with an audit client and the current status thereof. The IESBA issued an Exposure Draft in August 2014, in which they had proposed that the cooling-off period remain at two years for the EQC reviewer on the audit of PIEs. Although there was support from respondents for this, other respondents called for a longer cooling-off period, including the IESBA Consultative Advisory Group (CAG). Accordingly, in February 2016, the IESBA published their re-Exposure Draft (re-ED), *Limited Re-exposure of Proposed Changes to the Code Addressing the Long Association of Personnel with an Audit Client*, proposing that the cooling-off period for the EQC reviewer should be increased to 5 years for the audit of a listed and 3 years for the audit of a non-listed PIE. In response to the feedback on the re-ED, the IESBA has tentatively agreed at its June 2016 meeting on a revised cooling-off period of 3

⁹¹ IES 8 (Revised), *Professional Competence for Engagement Partners Responsible for Audits of Financial Statements*

years for EQCRs on the audits of all PIEs. The wording for the revised provisions is contained in Appendix 1. However, the IESBA did not address the cooling-off period relating to the time that an individual who had previously been involved in the audit, including in the role of the engagement partner, would not be eligible to fill the role of the EQC reviewer.

77. The explanatory memorandum to the IESBA's re-ED indicated that the determination of whether a cooling-off period should be served before a key audit partner could become the EQC reviewer is a matter that would be better addressed under ISQC 1. The IESBA is of the view that ISQC 1 already establishes requirements for the firm to establish policies and procedures to address the appointment of EQC reviewers and establish their eligibility, as well as to maintain the objectivity of the EQC reviewer. Accordingly, the IESBA is of the view that this matter should be considered as part of the IAASB's current initiative to review ISQC 1.
78. The WG is of the view that it is important for the IAASB to coordinate with the IESBA on this matter, to ensure that a consistent and practical approach is established across the standard-setting boards.
79. The WG debated where provisions addressing the period of time that an individual who had previously been involved in the audit would not be eligible to fill the role of the EQC reviewer would be best placed, i.e., in the IAASB's standards or in the IESBA Code. The WG had differing views regarding the appropriate location as follows:
- This matter would be best addressed in ISQC 1. ISQC 1 addresses the appointment of the EQC reviewer and the determination of whether or not an individual qualifies for appointment, through considering their objectivity in relation to the engagement. The cooling-off provisions in the IESBA Code address the threat to an individuals' objectivity in relation to the client, arising from being associated with a client over a period of time, which is not the same as addressing their objectivity in the context of performing an EQC review (i.e., having the ability to perform an objective evaluation of the judgments of the engagement team).
 - This matter would be best addressed by the IESBA. Although extant ISQC 1 contains provisions related to the objectivity of the EQC reviewer and the WG will be exploring how these provisions can be improved and clarified, the intent and purpose of the IAASB's standards is to address the competencies of the EQC reviewer and establishing requirements to ensure that the appropriate person is selected. The purpose is not to address the principles of objectivity further as this is a fundamental principle of the IESBA Code. Furthermore, the IAASB's standards do not currently address cooling-off periods in any other role, for example, the engagement partner. Locating cooling-off considerations in the IAASB's standards could create complexities for firms to navigate the provisions of the IAASB's standards, the IESBA Code and any local jurisdictional requirements.
80. The Steering Committee also discussed this matter and is of the view that while there may be elements that the IAASB could potentially address, there are other aspects that may be better addressed by the IESBA. That is, the elaboration of what is appropriate in terms of being able to demonstrate sufficient objectivity to perform the EQC review is a matter for which the IESBA's expertise is required. For example, if a specific cooling off period was to be prescribed, the IESBA is likely best placed to do so having considered threats to objectivity in more detail, and also likely having a view on how the self-review threat should be addressed. In contrast, the IAASB can address qualification matters such as required competencies of the EQC reviewer.

81. On the other hand, the EQC review function is a mechanism established by ISQC 1, and sets out requirements for firms to establish related policies and procedures. Accordingly, the IAASB could therefore seek to address the issue by further framing the concept of eligibility of an individual to serve as an EQC reviewer as potentially being affected by whether the individual had previously served on the engagement and the time that had elapsed.
82. The Steering Committee did not believe this matter needed to be addressed immediately by the IESBA through its Long Association project, but recognized that it is a matter that cannot remain unaddressed in either the IAASB's Standards or the IESBA Code and that any steps forward should be consistent with the respective board's remits. It recommended that the IESBA be informed of the developing views, and that appropriate coordination be determined once the WG and the IAASB's discussions have further advanced.
83. The WG will further explore options in view of respondents' feedback, including whether (i) a prescriptive period may be appropriate (in which case further consideration by the IESBA may be needed), (ii) there should be a requirement for the firm to establish a policy regarding a cooling-off period (that could include application material that recommends a minimum period, similar to the current approach in ISQC 1 regarding engagement inspections), or (iii) a more flexible approach would be appropriate whereby the objectivity of the EQC reviewer is considered in light of the risks in the circumstances.
84. In relation to the interaction with the IESBA, application material could be included in ISQC 1 that draws attention to the requirements in the IESBA Code addressing long association of senior personnel and the independence of the EQC reviewer. This would be consistent with recent projects of the IAASB where reference to the IESBA Code has been made, such as non-compliance with laws and regulations and ISA 260 (Revised). If the WG believes a prescriptive period may be appropriate, it would be helpful to further coordinate with IESBA to determine where this should be placed.

Matters for CAG Consideration

6. The CAG Representatives and Observers are asked to share their views regarding the WG's initial proposals addressing the eligibility of the EQC reviewer, in particular:
 - (a) The appropriateness of the additional requirements that would be established for listed entities.
 - (b) The knowledge and competence that is required to serve as the engagement partner on the audit that would be considered relevant to the performance of the EQC review.
7. With regard to the cooling-off period for an engagement partner to an EQC reviewer:
 - (a) Do the CAG Representatives and Observers agree with the WG's proposal that the IESBA be informed of the developing views, and that appropriate coordination be determined once the WG and the IAASB's discussions have further advanced?
 - (b) The CAG Representatives and Observers are asked to share their views regarding whether (i) a prescriptive period is appropriate, (ii) it should be a requirement for the firm to establish a policy regarding a cooling-off period, or (iii) a more flexible risk-based approach is appropriate.

E. *Separate EQC Review Standard*

Background

85. Given the importance and value placed on the role of the EQC review by stakeholders, particularly investors and regulators, the ITC requested views from respondents regarding whether a separate EQC review standard would be appropriate to give further prominence to, and emphasize the importance of, the EQC review.

Feedback from Respondents

86. Only one member of the MG⁹² responded to this question, and supported a separate standard due to the cross-cutting nature of the topic.
87. Other regulators and audit oversight authorities⁹³ did not support a separate standard, as it would give undue prominence to the EQC review in relation to other important factors in quality control and could dilute accountability and shift responsibility away from the engagement partner. One regulator and audit oversight authority⁹⁴ was indifferent regarding the location of the EQC reviews in a separate standard, but highlighted that the EQC review is a firm level control and accordingly should be in ISQC 1 or a new standard in that series, and should not be in ISA 220.
88. Respondents from NSS and member bodies⁹⁵ highlighted that there were different views on this subject arising from their outreach. Supporters spanning many stakeholder groups⁹⁶ indicated that a separate standard would clarify the EQC review requirements and responsibilities of the EQC reviewer and elevate the importance of the EQC review. Non-supporters, also representative of a range of stakeholder groups,⁹⁷ raised concern with a separate standard, including:
- It would create disproportion in terms of the responsibilities of the EQC reviewer and engagement partner.
 - The EQC review is only one element of the system of quality control and therefore should not have special prominence.
 - The current structure of the IAASB standards is appropriate, whereby requirements for firms to develop policies and procedures related to EQC reviews are located in ISQC 1 and performance requirements for EQC reviewers are located in ISA 220.

⁹² MG: IAIS

⁹³ Other Regulators and Audit Oversight Authorities: IRBA, MAOB

⁹⁴ Other Regulators and Audit Oversight Authorities: UKFRC

⁹⁵ NSS: AUASB, CAASB; Member Bodies and Other Professional Organizations: SAICA

⁹⁶ Accounting Firms: BDO, CHI, DTT; Public Sector Organizations: AGC, AGSA, GAO, INTOSAI; Member Bodies and Other Professional Organizations: FSR; Individuals and Others: JGrant

⁹⁷ NSS: CNCC-CSOEC, IDW, NBA, NZAuASB; Accounting Firms: EYG, GTI, KPMG; Member Bodies and Other Professional Organizations: ACCA, AICPA, APESB, CAANZ, CAI, CPAA, FEE, IRE-IBR, ICAEW, ICAS, ICAZ, ICPAK, ISCA, SMPC, WPK; Individuals and Others: DAHughes, SDeViney

There were also respondents⁹⁸ who indicated that they were indifferent as to where the EQC review requirements should be located, or that the consideration of whether a separate standard is needed would depend on the complexity and volume of the enhanced proposals relating to the EQC review.⁹⁹

89. An accounting firm¹⁰⁰ indicated that although the EQC review is a firm level control, the actual role is at an engagement level and the current construct of ISQC 1 may have the unintended consequence of mixing concepts relating to firm level and engagement level issues.
90. A member body¹⁰¹ recommended that a summary of the requirements relating to the EQC review could be developed, for example, in an Appendix to ISQC 1 or an IAASB Staff Audit Practice Alert, and that this could be used as a way of promoting the role of the EQC reviewer and the importance of being involved at the right time or to the right extent when conducting an EQC review.

WG Views and Matters for Further CAG Consideration

91. The WG noted the mixed views regarding whether a separate standard should be developed for EQC reviews. The WG revisited the original reasons why relocating the EQC review to a separate standard would be beneficial, i.e., to bring additional prominence to the contribution of the EQC review, to allow for greater elaboration of the requirements and application material supporting EQC reviews and to address the scalability of ISQC 1.
92. Although respondents were overall less supportive of a separate standard, the WG is of the view that the necessity for a separate standard will only be clear once the WG has considered all of the issues relating to EQC reviews, in particular the complexity and volume of the enhanced proposals and how these integrate with a QMA. This consideration will be further impacted by the IAASB's decision as to whether it is appropriate to separate ISQC 1 into three standards as further discussed in **Agenda item G.1**.

Matter for CAG Consideration

8. Do the CAG Representatives and Observers agree with the WG's recommendation that a separate EQC review standard should be considered at a later stage once the WG has considered the remaining issues regarding EQC reviews and the impact of three separate ISQC standards (should the IAASB determine this to be an appropriate way forward)?

⁹⁸ NSS: JICPA, MAASB; *Accounting Firms*: PWC

⁹⁹ *Accounting Firms*: RSM; *Member Bodies and Other Professional Organizations*: KICPA

¹⁰⁰ *Accounting Firms*: BDO

¹⁰¹ *Member Bodies and Other Professional Organizations*: APESB

Appendix 1

IESBA Proposals Regarding Cooling-Off

The IESBA proposals below have been extracted from [Agenda Item 6-C](#), presented to the IESBA Board in June 2016.

General Provisions

- 290.152 If a firm decides that the threats are so significant that rotation of an individual is a necessary safeguard, the firm shall determine an appropriate period during which the individual shall not be a member of the engagement team, provide quality control for the audit engagement, or exert direct influence on the outcome of the audit engagement. The period shall be of sufficient duration to allow the familiarity and self-interest threats to independence to be eliminated or reduced to an acceptable level. In the case of a public interest entity, paragraphs 290.153 to 290.168 also apply.

Audits of Public Interest Entities

- 290.153 In respect of an audit of a public interest entity, an individual shall not act in any of the following roles for a period of more than seven years (the “time-on” period):

- (a) The engagement partner;
- (b) The key audit partner responsible for the engagement quality control review where appointed pursuant to the requirements of ISQC 11 or law or regulation; or
- (c) Any other key audit partner role.

After the time-on period, the individual shall serve a cooling-off period in accordance with the provisions in paragraphs 290.154 – 290.162.

Cooling-off Period

- 290.154 If the individual acted as the engagement partner for seven years, the cooling-off period shall be five consecutive years.
- 290.155 Where the individual has been appointed as a key audit partner responsible for the engagement quality control review pursuant to the requirements of ISQC 1 or law or regulation and has acted in that capacity for seven years, the cooling-off period shall be three consecutive years.
- 290.156 If the individual has acted in any other capacity as a key audit partner for seven years, the cooling-off period shall be two consecutive years.