

Eligibility of the Engagement Quality Control Reviewer — Issues and Task Force Recommendations**Objective of the IAASB Discussion**

The objective of this Agenda item is to obtain the IAASB's feedback on the Quality Control Task Force (QCTF's) recommendations in relation to the eligibility of the engagement quality control (EQC) reviewer, in response to the IAASB's feedback at the September 2016 meeting.

Introduction

1. At the September 2016 IAASB meeting, the QCTF presented their initial proposals on matters related to EQC reviews, including the eligibility of the EQC reviewer, in response to the feedback from respondents to the Invitation to Comment, *Enhancing Audit Quality in the Public Interest: A Focus on Professional Skepticism, Quality Control and Group Audits* (ITC). At the December 2016 IAASB meeting, the QCTF presented their recommendations on the proposed revisions to ISQC 1¹, on the following matters related to EQC reviews:

- (a) Setting the objective of an EQC review;
- (b) Revising the definition of an EQC review;
- (c) Determining the scope of the engagements subject to an EQC review; and
- (d) The execution of an EQC review.

An extract of the IAASB's September 2016 discussions is available in Appendix 2 to this paper.

2. This paper incorporates the QCTF's proposed revisions to ISQC 1 in relation to the eligibility of the EQC reviewer, which includes the QCTF's recommendations to address 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 (the cooling-off period). Table 1 includes the proposed requirements and application material in relation to the QCTF's recommendations.
3. In developing these proposals, the QCTF considered the purpose and application of the EQC review in light of the revised quality management approach being adopted in ISQC 1. The QCTF recognized that an EQC review is only one of many possible responses that the firm may identify to address quality risks, for example, the firm may perform other types of reviews that are more focused on specific types of risks or the firm may identify other controls to address quality risks. The QCTF notes that the intention of the EQC review is that it is undertaken to address quality risks in relation to engagements that would have a significant impact in the event of a failure, for example, listed entities, engagements that have characteristics similar to listed entities or other engagements identified by the firm that have certain risk characteristics. Accordingly, the QCTF's recommendations in relation to the eligibility of the EQC reviewer were formed in this context.

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

Task Force Recommendations

Criteria for Selection of an EQC Reviewer

4. At its September 2016 meeting, the IAASB supported the recommendations of the QCWG relating to the criteria for the selection of the EQC reviewer, although the IAASB cautioned that these should not be overly prescriptive resulting in firms having limited suitable resources who are able, or willing, to fulfill the role. The IAASB also provided the following suggestions:
 - (a) Emphasize that the EQC reviewer needs to have the appropriate authority and status to enable them to confidently challenge the significant judgments.
 - (b) Address the appropriateness of the EQC reviewer's practical experience, for example, circumstances when the EQC review is delegated to a technical resource with limited practical experience.
 - (c) Address the capacity of the EQC reviewer to perform the review, i.e., their time available.
 - (d) Address the appropriate skills of the EQC reviewer.
5. In considering the attributes necessary for the EQC reviewer to be suitably qualified to fulfill the role, the QCTF researched other standards or regulations that address the attributes of the EQC reviewer, as well as the attributes that apply to engagement partners and professional accountants which could apply to the EQC reviewer, including the following:
 - (a) International Education Standard 8 (IES 8)² establishes the professional competence professional accountants develop and maintain when performing the role of an engagement partner. The three main competence areas set up in IES 8 are: (1) technical competence, (2) professional skills and (3) professional values, ethics and attitudes.
 - (b) The Code of Ethics for Professional Accountants issued by the International Ethics Standards Board for Accountants (IESBA Code) sets up the fundamental principles the professional accountant shall apply. Those principles are: (1) integrity, (2) objectivity, (3) professional competence and due care, (4) confidentiality and (5) professional behavior.
 - (c) Article 8 of the Regulation No 537/2014 of the European Parliament and of the Council (the EU Regulation) contains criteria for the EQC reviewer including that the reviewer shall be (1) a statutory auditor who is (2) not involved in the performance of the statutory audit to which the review relates. Several criteria exist for statutory auditors (such as educational qualifications and professional competence) in the EU legislation (amended Directive 2006/43/EC of the European Parliament and of the Council).
 - (d) The PCAOB Auditing Standard No. (AS) 7 requires that the EQC reviewer must be a partner or another individual in an equivalent position. AS 7 includes criteria such as independence, integrity and objectivity, but also addresses the competency of the EQC reviewer, being that they have the level of knowledge and competence related to accounting, auditing and financial reporting that is required to serve as the engagement partner on the engagement under review.

² International Education Standard 8 (IES 8) on Professional Competence for Engagement Partners Responsible for Audits of Financial Statements (Revised)

AS 7 also states that the person who served as the engagement partner during either of the two audits preceding the audit subject to engagement quality review may not be the engagement quality reviewer.

6. The QCTF debated these attributes, taking into consideration the feedback from respondents to the ITC and the views of the IAASB at its September 2016 meeting, and identified the following attributes as necessary in order for an individual to be eligible to perform the EQC review:
- (a) *Appropriate authority*—Paragraph 39 of ISQC 1 indicates that the EQC reviewer needs to have the necessary authority. The QCTF recognizes the concerns of respondents and the IAASB that having the appropriate authority is absolutely essential to the effectiveness of the EQC review. However, the QCTF is of the view that the term “appropriate authority” could be taken to mean that the EQC reviewer must have a particular title or position within the firm, for example, being at the same or higher level within the firm’s hierarchy. The QCTF noted that the purpose of appropriate authority is to establish the ability of the EQC reviewer to confidently challenge the significant judgments made by the engagement team, which would be achieved through the firm establishing the right culture that supports the EQC reviewer in undertaking their role. This in turn would lead to a situation where the engagement team, including the engagement partner, has professional respect for the EQC reviewer and considers the EQC reviewer as a person who can raise appropriate challenges. There are various ways that a firm can establish such a culture and support for the EQC reviewer, for example, the firm may identify a senior individual within the firm who oversees the EQC review process, or the firm’s processes for addressing differences of opinion may be helpful. As proposed to the IAASB in December 2016, one of the components of quality management would be “*organization, culture and strategy that foster quality.*” The QCTF notes that this would also be important to establishing a “culture” that supports the EQC reviewer. (See paragraph A46a–A46b of Table 1)
 - (b) *Technical competence*—Paragraph 39 of ISQC 1 includes technical qualifications as a necessary attribute to be eligible to perform the EQC review, however, the term “qualifications” is not defined in ISQC 1. “Technical competence” is defined in the IAESB *Glossary of Terms* as “the ability to apply professional knowledge³ to perform a role to a defined standard”. The QCTF is of the view that the term “qualifications” appears limited to the education of the EQC reviewer, rather than all-encompassing of the person’s knowledge and ability to apply such knowledge. Furthermore, throughout the ISAs, “competence” is used in relation to the knowledge, experience and skills of the engagement team. Accordingly, the QCTF is of the view that the phrase “technical qualifications” should be replaced with “technical competence”. The QCTF debated whether it would be appropriate to prescribe that the EQC reviewer needs to have the technical competence which is required to serve as the engagement partner on the audit, similar to the approach in AS 7 (see paragraph 5(d)). However the QCTF concluded that the necessary level of competence varies depending on the circumstances of the engagement and that such a requirement may be too restrictive as there could be circumstances where this would not be practicable. Instead, the application material would provide examples of what is

³ “Professional knowledge” is defined in the IAESB *Glossary of Terms* as “Those topics that make up the subject of accountancy as well as other business disciplines that, together, constitute the essential body of knowledge for professional accountants.”

meant by “technical competence”, for example, similar to the examples in paragraph A11 of ISA 220. (See paragraphs 39(a), A47 and A47c–A47d of Table 1)

- (c) *Capacity*—As proposed to the IAASB in December 2016, more emphasis has been brought to the timeliness of the EQC review in addressing the objective of the EQC review, and the nature, timing and extent of the EQC review procedures. In order to echo the importance of performing the EQC review procedures at appropriate stages during the engagement, the QCTF is of the view that the capacity of the individual to perform the EQC review needs to be addressed. Paragraph 30 of ISQC 1 sets the requirement for engagement partners to have the appropriate capabilities to perform their role, while paragraph A30 explains that firms should monitor the workload and availability of engagement partners so as to enable them to have sufficient time to discharge their role. The QCTF is of the view that similar guidance is helpful in relation to the capacity of the EQC reviewer. (See paragraphs 39(a) and A47a of Table 1)
- (d) *Practical experience*—Paragraph 39 of ISQC 1 also mentions having the necessary experience to perform the role of the EQC reviewer. In light of the views of the IAASB regarding the importance of having an appropriate level of experience in performing the role, the QCTF recommends that it be separated from technical competence. In addition, the QCTF is of the view that for audits of financial statements of listed entities, the requirement needs to specify that such experience should include experience related to an audit of financial statements of a listed entity (i.e., the individual was previously involved in an audit of a listed entity, e.g., as an engagement partner, an assistant partner or senior engagement team member). This is necessary in clarifying the minimum expectation for such engagements and ensuring that the EQC reviewer is suitable. Furthermore, in order to respond to the views of respondents, the application material would explain the importance of the firm considering inspection results or other performance ratings related to engagement quality of the proposed EQC reviewer. (See paragraphs 39(b) and A47b–A47d of Table 1)
- (e) *Objectivity*—Paragraph 20 of ISQC 1 requires the firm to establish policies and procedures addressing compliance with relevant ethical requirements by the firm and its personnel (including the EQC reviewer). This is supported by application material which references the fundamental principles of the IESBA Code, which includes the principle of objectivity. **Appendix 1** of this Agenda Item provides an explanation of how the principles in the IESBA Code relate to the objectivity of the EQC reviewer, with a focus on self-review threats, self-interest threats and familiarity threats that may arise in the context of the EQC reviewer’s role when performing the EQC review. Other relevant ethical requirements may also apply to the EQC reviewer, for example, ethical requirements established in the firm’s jurisdiction. Paragraphs 7–15 below further discuss the objectivity of the EQC reviewer, including the time that an individual who had previously served as engagement partner would not be eligible to fulfill the role of the EQC reviewer (cooling-off period). (See paragraphs 39(c) and A47e–A47k of Table 1)

Matter for IAASB Consideration

1. The IAASB is asked to share their views regarding the proposals in relation to the eligibility of the EQC reviewer, in particular:
 - (a) Does the IAASB agree with how the authority of the EQC reviewer would be emphasized in ISQC 1? (See paragraphs A46a–A46b of Table 1)
 - (f) Does the IAASB agree with the proposal that technical competence is a required attribute of the EQC reviewer, and that the characteristics of technical competence would be explained in application material? (See paragraphs 39(a), A47 and A47c–A47d of Table 1)
 - (b) Does the IAASB agree with the proposal that the capacity of the individual to perform the EQC review needs to be addressed in ISQC1? (See paragraphs 39(a) and A47a of Table 1)
 - (c) Does the IAASB agree with the proposal for the inclusion of a specific requirement on relevant experience and if so, to what extent should the requirements be specific in relation to the nature and extent of that experience? (See paragraphs 39(b) and A47b–A47d of Table 1)

Objectivity

7. In considering the objectivity of the EQC reviewer, the QCTF considered how objectivity and threats to objectivity are defined and addressed in the IESBA Code. In doing so, the IAASB Staff, IESBA Staff, Chair of the QCTF and certain members of the IESBA Board discussed the application of the IESBA Code, particularly in light of IESBA's various projects that have been recently completed, or are underway. A detailed explanation of this is provided in **Appendix 1**. IESBA is particularly interested in the discussions of the IAASB in this regard, and intend to discuss the issues related to the objectivity of the EQC reviewer at their meeting in June 2017.
8. Paragraph 20 of ISQC 1 requires the firm to establish policies and procedures in relation to compliance by the firm and its personnel with relevant ethical requirements, and paragraph 25 requires the firm to establish policies and procedures addressing familiarity threats arising from long association of personnel that take into consideration relevant ethical requirements. Nevertheless, the QCTF is of the view that in order to enhance the firm's consideration of the objectivity of the EQC reviewer, that ISQC 1 needs to direct the firm to consider the requirements of law, regulation or relevant ethical requirements. In considering law, regulation or relevant ethical requirements, the firm may identify specific provisions that need to be applied in relation to long association with the client or a cooling-off period for an engagement partner that prohibits them from fulfilling the role of EQC reviewer for a certain period. (See paragraphs 39(c) and A47e of Table 1)
9. Although relevant ethical requirements address the principle of objectivity and the threats that may arise through the application of the fundamental principles, the QCTF is of the view that there are certain threats to objectivity that are unique to the EQC reviewer in the context of their role (i.e., in addition to the 'usual' threats that would be faced by a professional accountant in public practice which are explained in the IESBA Code). These include:

- (a) A self-review or self-interest threat may arise from being a previous member of the engagement team, in particular the engagement partner, or being recently consulted on matters related to the engagement where areas of significant judgment exist.
 - (b) A familiarity or self-interest threat may arise when the EQC reviewer is a close or immediate family member of the engagement partner, or another key member of the engagement team, as well as in circumstances when close personal relationships are developed through long association with such personnel.
 - (c) An intimidation threat may arise in circumstances when a member of the engagement team, including the engagement partner is an aggressive or dominant individual, or the EQC reviewer is in the chain of command of a member of the engagement team, including the engagement partner.
10. The IESBA Code does not specifically discuss the above threats in the context of the EQC reviewer although, in the view of the IESBA, they are covered by the fundamental principles. However, the QCTF agrees that there is insufficient granularity in the IESBA Code in terms of specifically explaining how these threats may arise in the case of an EQC reviewer and how such a threat could be adequately safeguarded. As a result, absent such threats being explicitly addressed in the IESBA code, the QCTF is of the view that the application material supporting the requirements that address the objectivity of the EQC reviewer would need to explain these threats in order that firms consider whether, or how these apply, in evaluating the objectivity of the EQC reviewer. (See paragraphs A47f–A47i of Table 1)

Cooling-off period

11. The QCTF considered the circumstances when law, regulation or relevant ethical requirements do not explicitly prohibited a former engagement partner from fulfilling the role of an EQC reviewer. In particular, the QCTF identified that a self-review or self-interest threat may exist in such circumstances, and that without a requirement in place which prescribes a cooling-off period (i.e., the time that an individual who had previously served as engagement partner would not be eligible to fill the role of the EQC reviewer), EQC reviewers may not be sufficiently objective. Accordingly, the QCTF is of the view that a requirement needs to be established for a cooling-off period in respect of audits of financial statements in order to address the proper performance of the EQC review in the public interest. In relation to engagements other than audits of financial statements, the QCTF is of the view that the risk of a self-review or self-interest threat may vary depending on the circumstances of the engagement and establishing a fixed cooling-off period in relation to these other types of engagements may be inappropriate.
12. The QCTF considered whether such a requirement should be incorporated into ISQC 1, or whether it would be best addressed by IESBA. The QCTF observed that respondents to the ITC overall supported actions to address the cooling-off period, however there were mixed views as to whether it should be addressed by the IAASB, IESBA or both.
13. In relation to addressing familiarity threats to the EQC reviewer's independence, respondents to the IESBA's Exposure Draft, [*Limited Re-Exposure of Proposed changes to the Code Addressing the Long Association of Personnel with an Audit Client*](#) (Limited Re-ED), suggested locating the provisions relating to the long association of EQC reviewers with an audit client in ISQC 1. However,

the IESBA concluded that this would be inappropriate given that independence is within the remit of IESBA (see [Basis for Conclusions: Changes to the Code Addressing Long Association](#) (BFC)). Although a familiarity threat is different from a self-review or self-interest threat, the principles in relation to where provisions are located in the IESBA Code versus ISQC 1 are analogous and should be applied consistently.⁴ The QCTF further noted in the BFC that the IESBA committed to future coordination with the IAASB in respect of EQC reviewers on matters arising in relation to the review of ISQC 1.

14. The QCTF agreed that the requirement for a cooling-off period (i.e., that prohibits a person who served as an engagement partner on an audit of financial statements from filling the role of the EQC reviewer on that engagement) would be best placed in the IESBA Code. Given the planned discussion by the IESBA at their June 2017 meeting, the QCTF is of the view that further coordination with IESBA is needed before finalizing the requirements in relation to the cooling-off period. Nevertheless, members of the QCTF are of the view that the IAASB may need to pursue addressing the cooling-off period in ISQC 1, in light of the time it may take IESBA to undertake the changes to the IESBA Code if IESBA determines this to be the appropriate course of action. However, one member of the QCTF is of the view that ISQC 1 should not be used as a mechanism to address matters that are within the ambit of the IESBA Code, and that it should be left to IESBA to address, irrespective of the time it would take to do so.
15. In light of the QCTF's views that a cooling-off period should be established (either in ISQC 1 or the IESBA Code), the QCTF debated an appropriate period for the cooling-off period. The QCTF noted the requirement in the PCAOB's standard AS 7 that prescribes a 2 year cooling-off period. The QCTF is of the view that it is highly unlikely that a cooling-off period shorter than 2 years would be appropriate, because decisions that the engagement partner makes in an audit of financial statements usually has an effect for at least two years following that financial period. The QCTF also noted in IESBA's BFC that a period of 3 years was considered appropriate in relation to the cooling-off period for an EQC reviewer under the long association provisions because this would better ensure that the individual would be away from the audit engagement for a full 2 financials years, given the "hand-over" process that can occur at the end and beginning of an audit, thereby better supporting the "fresh look" principle.

Other Considerations

16. The QCTF noted the views of the Board that the function of the EQC reviewer needs to be reinforced, i.e., the EQC reviewer should critically evaluate and challenge the judgments, decisions and conclusions of the engagement team and the engagement team should evaluate how best to address the issues raised by the EQC reviewer. However, the engagement team should not rely on the EQC reviewer to make decisions and judgments. In circumstances when there are differences of opinion between the EQC reviewer and the engagement team, the firm would have established processes

⁴ In the Limited Re-ED, the IESBA noted the following in relation to a possible cooling-off period from being an engagement partner to an EQC reviewer: "The IESBA determined that if a cooling-off period is to be served before a key audit partner could become an EQC reviewer, this matter would be best addressed under ISQC 1. The IESBA noted that ISQC 1 already establishes requirements for the independence and objectivity of the EQCR". The QCTF noted that this conclusion was prior to the IESBA's conclusion on the appropriate location of the long association provisions addressing familiarity threats, which is a similar issue, and therefore it is evident that the IESBA's thinking on this has evolved since the Limited Re-ED.

for addressing differences of opinion. This concept is addressed in paragraph A49 of the extant ISQC 1 (the EQC reviewer does not make decisions for the engagement team), however further application material will be included to emphasize this. (See paragraph A47j of Table 1)

Matters for IAASB Consideration

2. The IAASB is asked to share their views in relation to the objectivity of the EQC reviewer, in particular:
 - (a) Does the IAASB agree with the QCTF's proposal to enhance the application material in relation to threats to objectivity that are unique to the EQC reviewer in the context of their role? (See paragraphs A47f–A47i of Table 1)
 - (b) Does the IAASB agree that a fixed cooling-off period needs to be established in respect of audits of financial statements?
 - (c) Is the IAASB of the view that ISQC 1 should include a cooling-off period if it is determined by the IESBA that the cooling-off period will not be incorporated into the IESBA Code within the foreseeable future?
 - (d) Does the IAASB have any views regarding the period of the cooling-off period, for example, should the approach of the PCAOB be followed (2 years), or would it be more appropriate to align with the IESBA provisions addressing the long association of the EQC reviewer (3 years)?

The Process for the Selection of the EQC Reviewer (Paragraphs 41 and A49–A50 of Table 1)

17. The IAASB agreed at the September 2016 meeting that the EQC review is a firm-level control that operates at an engagement level, and this has been incorporated into the proposed objective of an EQC review that was presented to the Board at its December 2016 meeting. Furthermore, the IAASB was of the view that members of the firm other than those involved in the engagement should select the EQC reviewer, given that the EQC review is a firm level control. However, this is not always possible, for example, in smaller firms where there are very few engagement partners. Under paragraph A49 of extant ISQC 1, the selection of the EQC reviewer is undertaken by the firm, *where practicable*. The QCTF proposes enhancing this by including a requirement that the EQC reviewer shall be selected by someone other than the engagement partner or other members of the engagement team unless in exceptional circumstances it is not possible, with application material explaining that, in circumstances when there is no one other than the engagement partner or a member of the engagement team to select the EQC reviewer, other mechanisms are established to safeguard the objectivity of the EQC reviewer. (See paragraphs 41b and A50 of Table 1)
18. The QCTF further recommends that the application material should explain how the requirements relating to the eligibility of the EQC reviewer would apply in circumstances when the firm selects an EQC reviewer outside from the firm. The QCTF noted the PCAOB's guidance contained in the overview section to the release of the Engagement Quality Review Standard⁵ in developing the application material proposed in paragraph A50 of Table 1.

⁵ https://pcaobus.org/Rulemaking/Docket%2025/2009-07-28_Release_No_2009-004.pdf

19. In addition, the QCTF is of the view that those responsible for selecting the EQC reviewer need to have sufficient knowledge to be able to assess whether individuals are eligible to perform the EQC review, which includes knowledge of the individuals as well as knowledge about the engagements that are subject to an EQC review. These qualities are essential in ensuring that the right person is performing the review. Accordingly, the QCTF proposes introducing a new requirement that sets out the qualities of the person assigned the function of selecting the EQC reviewer. (See paragraphs 41a and A49 of Table 1)

Matters for IAASB Consideration

3. Does the IAASB agree with the approach regarding the selection of the EQC reviewer, i.e.:
- (a) The person selecting the reviewer should be someone other than the engagement partner or other members of the engagement team, with an exception for circumstances when this is not practicable. (See paragraphs 41b and A50 of Table 1)
 - (b) Those responsible for selecting the EQC reviewer need to have sufficient knowledge to be able to assess whether individuals are eligible to perform the EQC review. (See paragraphs 41a and A49 of Table 1)

Table 1: Proposed Requirements and Application Material Addressing the Selection and Eligibility of the EQC reviewer (changes represent the “marked from extant”)

Requirements

Criteria for the Eligibility of Engagement Quality Control Reviewers

39. ~~The firm shall establish policies and procedures to address the appointment of engagement quality control reviewers and establish their eligibility through:~~ The firm’s policies and procedures that establish the criteria for the eligibility of the engagement quality control reviewer, shall be designed to enable the engagement quality control reviewer to provide an objective evaluation, in a timely manner at appropriate stages during the engagement, of the significant judgments made by the engagement team and the conclusions reached thereon. Such policies and procedures shall include that the engagement quality control reviewer: (Ref. Para: A46a–A46b)
- (a) Has sufficient technical competence, including knowledge of the entity’s industry, and capacity to be able to perform the role of engagement quality control reviewer for the particular engagement; (Ref. Para: A47–A47a and A47c–A47d) ~~The technical qualifications required to perform the role, including the necessary experience and authority; and (Ref: Para. A47);~~
 - (b) Has appropriate experience related to engagements of a similar nature and complexity, and in the case of an engagement quality control review for an audit of financial statements of a listed entity, appropriate experience related to an audit of financial statements of a listed entity; and (Ref. Para: A47b–A47d) ~~The degree to which an engagement quality control reviewer can be consulted on the engagement without compromising the reviewer’s objectivity. (Ref: Para. A48)~~
 - (c) Maintains their objectivity throughout the engagement, including complying with the requirements of law, regulation or relevant ethical requirements relating to objectivity, if any. (Ref.

Para: A47e–A47j) [Requirement to be further developed once further liaison with IESBA has taken place]

- ~~40. The firm shall establish policies and procedures designed to maintain the objectivity of the engagement quality control reviewer. (Ref: Para. A49–A51)~~
- ~~404. If during the engagement the engagement quality control reviewer’s objectivity may have become impaired or the engagement quality control reviewer’s ability to perform the review is otherwise determined to be impaired, tThe firm’s policies and procedures shall provide for the replacement of the engagement quality control reviewer where the reviewer’s ability to perform an objective review may be impaired. (Ref: Para. A48)~~
- ~~41. The firm shall assign the responsibility for the appointment of the engagement quality control reviewer(s) to an engagement(s) to an individual(s) who: (Ref: Para. A49-A50)~~
- ~~(a) Possesses sufficient knowledge to be able to assess whether the individual(s) is eligible to perform the engagement quality control review; and~~
 - ~~(b) Is not part of the engagement team unless, in exceptional circumstances, it is not practicable.~~

Application Material

Criteria for the Eligibility of Engagement Quality Control Reviewers (Ref: Para. 39)

~~A46a. Policies and procedures establish the responsibilities of the engagement quality control reviewer in undertaking their review, and form the basis for their ability to confidently challenge the significant judgments made by the engagement team and the conclusions reached thereon. The audit firm’s culture has an important influence on the values, ethics and attitudes of engagement partners and staff. A firm culture that fosters audit quality creates a culture where audit quality is valued and promotes the personal characteristics essential to audit quality, including where the engagement partner and engagement team have professional respect for the engagement quality control reviewer and consider the engagement quality control reviewer as a person who can raise appropriate challenges.~~

~~A46b. Other policies and procedures established by the firm may also help to promote a culture that respects the purpose of the engagement quality control review. For example, the firm’s policies and procedures addressing differences of opinion and appropriate consultation may be useful in promoting such a culture and assigning responsibility for the oversight of the engagement quality control review process to a senior individual within the firm may also promote this culture.~~

~~Sufficient and Appropriate Technical Competence Expertise, Capacity and Experience and Authority (Ref: Para. 39(a)–39(b))~~

~~A47. What constitutes sufficient and appropriate technical expertise, experience and authority depends on the circumstances of the engagement. For example, the engagement quality control reviewer for an audit of the financial statements of a listed entity is likely to be an individual with sufficient and appropriate and experience and authority to act as an audit engagement partner on audits of financial statements of listed entities. The technical competence that is necessary to be able to perform the role of engagement quality control reviewer will depend on the circumstances of the~~

engagement. For example, technical competence may include an understanding of professional standards and applicable legal and regulatory requirements, specialized knowledge of areas of accounting or auditing or expertise with relevant information technology.

A47a. The policies and procedures addressing the capacity of the engagement quality control reviewer may include systems to monitor the workload and availability of the engagement quality control reviewers to enable the firm to make an assessment as to which individuals have sufficient time to adequately discharge their responsibilities.

A47b. In establishing the policies and procedures addressing the appropriate experience of the engagement quality control reviewer, the firm may take into consideration various factors, for example, the nature of the engagement and the entity, or the appropriate level of practical experience needed to be able to challenge the significant judgments made by the engagement team and the conclusions reached thereon (e.g., the individual has previously performed the role of engagement partner, engagement quality control reviewer or another senior role on a similar engagement).

A47c. The level of industry knowledge and experience that is sufficient to perform the role of engagement quality control reviewer depends on the engagement and the nature of the industry. For example, certain industries are highly specialized and have more complex accounting practices and would require greater industry expertise.

A47d. The policies and procedures addressing the eligibility of the engagement quality control reviewer may set out additional considerations in relation to the technical competency and experience of the engagement quality control reviewer. For example, such policies may take into consideration the inspection results or other performance ratings related to engagement quality of the engagement quality control reviewer.

Objectivity of the Engagement Quality Control Reviewer (Ref: Para. 39(c))

[The application material below provides an example of possible matters that may be included in the application material, however may require alteration once further liaison with IESBA has taken place.]

A47e. Paragraph 20 [of extant ISQC 1] requires the firm to establish policies and procedures designed to provide it with reasonable assurance that the firm and its personnel comply with relevant ethical requirements. The IESBA Code establishes the fundamental principles of professional ethics, including objectivity. In complying with the fundamental principles, the engagement quality control reviewer may be subject to threats that may affect their objectivity, including self-review threats, self-interest threats, familiarity threats, advocacy threats and intimidation threats. The IESBA Code provides examples of safeguards that may be appropriate to address such threats.

A47f. Threats to the objectivity of the engagement quality control reviewer may arise in relation to the client engagement or engagement team, through a self-review, self-interest, familiarity or intimidation threat. For example, the IESBA Code discusses self-interest and familiarity threats that may arise as a result of long association as a member of the engagement team, including in the role of engagement quality control reviewer, in the context of:

- The entity, its operations or senior management; or

- The subject matter and subject matter information of the engagement (e.g., the financial statements on which the firm will express an opinion or the financial information which forms the basis of the financial statements).

Law, regulation or relevant ethical requirements may establish requirements that prohibit an individual who previously served as engagement partner from being eligible to perform the engagement quality control review for a certain period. For example, the IESBA Code contains requirements addressing the long association of senior personnel with a client that may prohibit an individual from performing the role of engagement quality control reviewer when the individual has served as the engagement partner or engagement quality control reviewer in relation to the engagement for a particular period of time.⁶

A47g. Examples of circumstances that may create a self-review, self-interest, familiarity or intimidation threat in respect of the engagement quality control reviewer's association with the engagement team include:

- (a) A self-review or self-interest threat may arise from being a previous member of the engagement team, in particular the engagement partner, or being recently consulted on matters related to the engagement where areas of significant judgment exist.
- (b) A familiarity or self-interest threat may arise when the engagement quality control reviewer is a close or immediate family member of the engagement partner, or another key member of the engagement team, as well as in circumstances when close personal relationships are developed through long association with such personnel.
- (c) An intimidation threat may arise in circumstances when a member of the engagement team, including the engagement partner is an aggressive or dominant individual, or the engagement quality control reviewer is in the chain of command of a member of the engagement team, including the engagement partner.

A47h. Examples of safeguards that may be appropriate in addressing intimidation threats to the engagement quality control reviewer's objectivity, include:

- (a) Designating a member of firm leadership to be responsible for overseeing the adequate functioning of the firm's policies and procedures related to engagement quality control reviews, or having the appointment of the engagement quality control reviewer approved by a member of firm leadership.
- (b) Establishing robust processes for addressing differences of opinion or establishing policies and procedures to encourage and empower the engagement quality control reviewer to communicate to senior levels within the firm any issue relating to the performance of the engagement quality control review.
- (c) Utilizing an engagement quality control reviewer from another network firm or region who is outside the chain of command of the engagement partner or other member of the engagement team.

⁶ See, for example, Section 290 and 291 of the IESBA Code.

A47i. In some circumstances, it may not be possible to eliminate or reduce to an acceptable level a self-review, familiarity or intimidation threat and therefore the firm will determine that the individual is not eligible to be appointed as the engagement quality control reviewer. In circumstances when there are no suitable individuals to perform the engagement quality control review within the firm, the firm may contract suitably qualified external persons to perform the engagement quality control review or the firm may use other firms to perform the review.

A47j. Paragraph 39(c) requires that the engagement quality control reviewer maintains their objectivity throughout the engagement. For example, in performing the engagement quality control review, the engagement quality control reviewer evaluates the significant judgments of the engagement team; the engagement team would consider how best to address the matters raised by the engagement quality control reviewer but the engagement quality control reviewer does not make such judgments.

Consultation with the Engagement Quality Control Reviewer (Ref: Para. ~~4039(b)~~)

A48. The engagement team, including the engagement partner, may consult the engagement quality control reviewer during the engagement, for example, to establish that a judgment made by the engagement ~~partner~~team will be acceptable to the engagement quality control reviewer. Such consultation avoids identification of differences of opinion at a late stage of the engagement and need not compromise the engagement quality control reviewer's eligibility to perform the role. Where the nature and extent of the consultations become significant the reviewer's objectivity may be compromised unless care is taken by both the engagement team and the reviewer to maintain the reviewer's objectivity. Where this is not possible, another individual within the firm or a suitably qualified external person may be appointed to take on the role of either the engagement quality control reviewer or the person to be consulted on the engagement.

Assessment of the Eligibility of the Engagement Quality Control Reviewer (Ref: Para. 41)

A49. The role of the person(s) within the firm who is assigned responsibility for the assessment of whether the individual(s) is eligible to perform the engagement quality control review will vary from firm to firm. The complexity of the firm's process may depend on a number of factors, for example, the structure of the firm and its size, whether the firm is a network firm, its geographical dispersion and the range of services it provides. Sufficient knowledge to be able to assess the eligibility of the potential engagement quality control reviewer includes an appropriate knowledge of the engagement subject to engagement quality control review, as well all of the criteria set out in paragraph 39 in relation to the engagement quality control reviewer.

A50. In certain circumstances, it may not be practicable for an individual, other than a member of the engagement team, to appoint the engagement quality control reviewer. In such cases, the firm may establish other procedures to safeguard the engagement quality control reviewer's objectivity, for example, the firm may contract suitably qualified external persons or other firms to perform the engagement quality control review. In circumstances when the firm contracts suitably qualified external persons to perform engagement quality control reviews or uses other firms to perform the review, the firm may need to make inquiries to obtain necessary information about whether the individuals charged with performing the reviews comply with all the criteria set out in paragraph 39. In these

circumstances, the engagement team may consider documenting their evaluation of the objectivity of the engagement quality control reviewer, in order to evidence that the objectivity was considered appropriate.

~~Objectivity of the Engagement Quality Control Reviewer (Ref: Para. 40)~~

~~A49. The firm is required to establish policies and procedures designed to maintain objectivity of the engagement quality control reviewer. Accordingly, such policies and procedures provide that the engagement quality control reviewer:~~

- ~~• Where practicable, is not selected by the engagement partner;~~
- ~~• Does not otherwise participate in the engagement during the period of review;~~
- ~~• Does not make decisions for the engagement team; and~~
- ~~• Is not subject to other considerations that would threaten the reviewer's objectivity.~~

~~Considerations specific to smaller firms~~

~~A50. It may not be practicable, in the case of firms with few partners, for the engagement partner not to be involved in selecting the engagement quality control reviewer. Suitably qualified external persons may be contracted where sole practitioners or small firms identify engagements requiring engagement quality control reviews. Alternatively, some sole practitioners or small firms may wish to use other firms to facilitate engagement quality control reviews. Where the firm contracts suitably qualified external persons, the requirements in paragraphs 39–41 and guidance in paragraphs A47–A48 apply.~~

~~Considerations specific to public sector audit organizations~~

~~A51. In the public sector, a statutorily appointed auditor (for example, an Auditor General, or other suitably qualified person appointed on behalf of the Auditor General) may act in a role equivalent to that of engagement partner with overall responsibility for public sector audits. In such circumstances, where applicable, the selection of the engagement quality control reviewer includes consideration of the need for independence from the audited entity and the ability of the engagement quality control reviewer to provide an objective evaluation.~~

Appendix 1

Consideration of How the Principles in the IESBA Code relate to the Objectivity of the EQC Reviewer

1. Paragraph R110.2⁷ of the proposed restructured IESBA Code⁸ (paragraph 100.5 of the extant IESBA Code) requires a professional accountant to comply with the fundamental principles set out in the IESBA Code, which includes objectivity.⁹ In complying with these fundamental principles, paragraph R120.6¹⁰ (new explicit requirement derived from paragraph 100.6 and 290.1 of the extant IESBA Code) requires professional accountants to identify threats to compliance with the fundamental principles, which may include self-review threats, self-interest threats, familiarity threats, advocacy threats and intimidation threats. For the purposes of this discussion, the focus is on self-review threats, self-interest threats and familiarity threats that may arise in the context of the EQC reviewer's role when performing the EQC review. Nevertheless, the EQC reviewer has a responsibility to apply all of the principles of the IESBA Code.

⁷ Proposed restructured Code Part 1 – Complying with the Code, Fundamental Principles and Conceptual Framework, Section 110, *The Fundamental Principles*

⁸ In January 2017, the IESBA announced the completion of the major first phase of its strategic project to restructure the IESBA. The proposed restructured IESBA Code would be retitled International Code of Ethics for Professional Accountants (Including International Independence Standards).

The IESBA also released three exposure drafts (EDs) with new proposals that will enhance and complete the fully restructured IESBA Code with strengthened ethics requirements for professional accountants. Highlights of the main improvements to date, including details of how the different work streams are being coordinated and related timelines, are set out in the January 2017 publication, [IESBA Update: Toward a Restructured International Code of Ethics](#).

IESBA has also made available on its [website](#) the restructured and revised portions of the IESBA Code it has agreed to so far. These, together with a Staff-prepared [Compilation of Proposed Restructured IESBA Code](#), Basis for Conclusions documents, mapping tables, and other resources, are intended to support stakeholders' timely adoption and implementation efforts, and consideration of the January 2017 EDs.

The Staff-prepared Compilation of Proposed Restructured IESBA Code combines the [agreed-in-principle texts](#) for Phase 1 of the Structure and Safeguards projects and the proposed texts relating to the [Structure ED-2, Improving the Structure of the Code of Ethics for Professional Accountants—Phase 2, Safeguards ED-2, Proposed Revision Pertaining to Safeguards in the Code—Phase 2 and Related Conforming Amendments](#), and the [Applicability ED, Proposed Revisions to Clarify the Applicability of Provisions in Part C of the Extant Code to Professional Accountants in Public Practice](#). The comment deadlines for comments are May 25, 2017 for the Structure ED-2 and April 25, 2017 for the Safeguards ED-2 and Applicability ED.

The references to the IESBA Code in this paper are to the proposed restructured IESBA Code (i.e., the sections or paragraphs in the Staff-prepared Compilation of Proposed Restructured Code). Furthermore, for the purposes of clarity, the references to the existing requirements of the IESBA Code have also been included in brackets and **grey text**.

⁹ Paragraph 110.1 of the proposed restructured IESBA Code defines objectivity as “not to compromise professional or business judgments because of bias, conflict of interest or undue influence of others”.

¹⁰ Proposed restructured Code Part 1, Section 120, *The Conceptual Framework*

Familiarity threats

2. A familiarity threat is described in paragraph 120.6 A3 (d) of the IESBA Code (paragraph 110.12 (d) of the extant IESBA Code) as “the threat that due to a long or close relationship with a client, or employer, a professional accountant will be too sympathetic to their interests or too accepting of their work”. Sections 540¹¹ (paragraphs 290.148-290.168 of the extant IESBA Code) and 940¹² (partially new requirement, partially restructured from section 291.137 of the extant IESBA Code) of the IESBA Code, which contain the provisions relating to the long association of personnel, address familiarity threats for professional accountants in public practice (PAPPs) performing audits and reviews of financial statements or other assurance engagements in relation to:
 - The client;
 - In the case of an audit, the client’s operations and senior management; or
 - The subject matter (financial statements) or subject matter information (financial information which forms the basis of the financial statements), i.e., the engagement.
3. For audits of public interest entities, Section 540 of the IESBA Code (paragraphs 290.148-290.168 of the extant IESBA Code) contains requirements and application material that prescribe the maximum period that an individual may serve on the engagement, including as EQC reviewer, as well as minimum cooling-off periods, that are intended to address such familiarity and self-interest threats. During the cooling-off period, an individual is prohibited from being involved in the client, including performing the role of EQC reviewer. However, Section 540 (paragraphs 290.148-290.168 of the extant IESBA Code) does not address the circumstances when the individual switches between various roles during the time-on period, for example, an individual is permitted to serve a maximum of 7 years and therefore may fulfill the role of engagement partner for 4 years and switch to the EQC reviewer for 3 years. In respect of audits of entities that are not public interest entities, the conceptual framework set out in Section 120 of the IESBA Code would apply to identifying, evaluating and addressing threats created from long association (see introduction paragraphs in Sections 540). Accordingly, although the long association provisions may prevent the engagement partner from fulfilling the role of EQC reviewer in certain circumstances in order to address a familiarity or self-interest threat, there are circumstances that may arise when this is not explicitly prohibited.
4. Furthermore, the long association provisions address familiarity threats in relation to the client, its management and the engagement. However, Sections 540 (paragraph 290.148-290.168 of the extant IESBA Code) and 940 (partially new requirement, partially restructured from section 291.137 of the extant IESBA Code) do not include provisions to deal with familiarity threats that may be created from situations that exist within the firm (e.g., the EQC reviewer is a close family member of the engagement partner).

¹¹ Proposed restructured Code Part 4A – Independence for Audits and Reviews, Section 540, *Long Association of Personnel (Including Partner Rotation) with an Audit Client*

¹² Proposed restructured Code Part 4B – Independence for Other Assurance Engagements, Section 940, *Long Association of Personnel with an Assurance Client*

5. As highlighted above, paragraph 120.6 A3 (d) of the IESBA Code (100.12 (d) of the extant IESBA Code) describes familiarity threats in the context of the “relationship with a ... employer”. The Applicability ED contains proposals¹³ to clarify that the provisions in Part C of the extant IESBA Code (i.e., those applicable to professional accountants in business (PAIB)) might be applicable to PAPPs in ethical situations not involving clients. Paragraph 200.6 A1 of the IESBA Code (paragraph 300.11 of the extant IESBA Code) provides examples of facts and circumstances that might create familiarity threats for a PAIB, in the context of the relationship with an employer (e.g., a professional accountant being responsible for the financial reporting of the employing organization when an immediate or close family member employed by the organization makes decisions that affect the financial reporting of the organization). Similarly paragraph 200.6 A1 (paragraph 300.11 of the extant IESBA Code) also contains examples of facts or circumstances that might create intimidation threats that may be relevant to an EQC reviewer. These examples may help provide guidance for EQC reviewers in dealing with familiarity threats that may be created within the engagement team (e.g., the EQC reviewer is a close family member of the engagement partner).
6. In essence, the IESBA (the IESBA Staff, and certain members of the IESBA Board) are of the view that a familiarity threat in relation to the client, its management, the engagement or the engagement team is addressed in the IESBA Code. While certain sections of the IESBA Code provide explicit requirements and application material for addressing familiarity threats (e.g., the long association provisions for audits of public interest entities), the application of the conceptual framework is relevant for other circumstances (specifically paragraphs R120.10–120.10 A2 (paragraph 100.9 of the extant IESBA Code)). However, the QCTF concur that the IESBA Code does not provide appropriate granularity in terms of specifically explaining how a familiarity threat in relation to the engagement team may arise in the circumstance of an EQC reviewer and how such a threat could be adequately safeguarded.

Self-review or Self-interest Threats

7. A self-review threat is described in paragraph 120.6 A3 (b) of the IESBA Code (paragraph 100.12 (b) of the extant IESBA Code) as “the threat that a professional accountant will not appropriately evaluate the results of a previous judgment made, or an activity performed by the accountant, or by another individual within the accountant’s firm or employing organization, on which the accountant will rely when forming a judgment as part of performing a current activity”. A self-interest threat is described in paragraph XXXX of the IESBA Code (paragraph 100.12 (a) of the extant IESBA Code) as “the threat that a financial or other interest will inappropriately influence the professional accountant’s judgment or behavior”.
8. In the case of an EQC reviewer, a self-review or self-interest threat may arise as a result of the EQC reviewer being previously involved in the engagement. For example, after serving as the engagement partner on an audit of financial statements, the objectivity of the individual may be impaired in subsequent financial periods in relation to areas of the engagement where the individual exercised

¹³ Paragraph R300.5 of the IESBA Code indicates that “where a PAPP is performing professional activities pursuant to the accountant’s employment or ownership relationship with the firm, there might be requirements and application material in Part 2 [Proposed restructured Code, Part 2, Section 200, *Application of Conceptual Framework – Professional Accountants in Business*] that are also applicable to those circumstances. If so, the PAPP shall comply with the relevant provisions”.

significant judgment, due to the fact that the judgments made in one financial period may have relevance in succeeding financial periods. The IESBA is of the view that this situation is covered by the IESBA Code through the application of the conceptual framework. However, the QCTF concur that the IESBA Code does not provide appropriate granularity in terms of specifically explaining how a self-review or self-interest threat that may arise in the circumstance of an EQC reviewer and how such a threat could be adequately safeguarded.

Extract of Minutes – IAASB 2016 September Meeting

SELECTION OF THE EQC REVIEWER

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

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

The Board was supportive of further liaison with the IESBA on the issue relating to the 'cooling-off' period between serving as the engagement partner and the EQC reviewer, although mixed views were expressed regarding whether a prescriptive period should be established. Those in support of a fixed period suggested 3 years or 5 years and indicated that it would prevent inconsistent application by firms, whereas those not supportive of a fixed period were of the view that there is no proper basis for establishing a fixed period.

IAASB CAG CHAIRMAN'S REMARKS

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

WAY FORWARD

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