



May 16, 2016

Ms. Kathleen Healy  
Technical Director  
International Auditing and Assurance Standards Board  
International Federation of Accountants  
585 Fifth Avenue – 14<sup>th</sup> Floor  
New York, NY 10017  
U.S.A.

Dear Ms. Healy:

**Re: Invitation to Comment – *Enhancing Audit Quality in the Public Interest: A Focus on Professional Skepticism, Quality Control and Group Audits***

The Canadian Auditing and Assurance Standards Board (AASB) is pleased to provide its comments on the International Auditing and Assurance Standards Board's (IAASB) Invitation to Comment (ITC), *Enhancing Audit Quality in the Public Interest: A Focus on Professional Skepticism, Quality Control and Group Audits*. In developing our response, we considered comments provided by our stakeholders. AASB staff held many meetings with various stakeholder groups from across Canada, and considered response letters received to the AASB's ITC. Appendix A indicates the groups with whom staff consulted, and the respondents to our ITC. In our response, "Canadian stakeholders" refers to those who provided us with input.

**Structure of our response**

Our response contains the following:

- **General comments** – This section sets out our reactions to the pervasive matters related to the ITC.
- **Overall comments on key topics** – This section covers our general comments more specifically related to each of the key topics in the ITC:
  - Professional skepticism;
  - Quality control; and
  - Group audits.
- **Responses to the specific questions** – Our responses to the specific questions in the ITC have been broken out into each of the key sections in Appendices B through E.

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## General comments

The AASB applauds the IAASB's efforts to tackle a number of challenging topic areas. Although the perceived necessity for changes to the standards may differ between these topics, the AASB has used this ITC to engage in insightful discussions with our Canadian stakeholders regarding audit quality more generally.

### Use of a combined approach

The IAASB used a new approach for this consultation in issuing one combined document, covering three key topics where feedback is being sought. While the AASB acknowledges the IAASB's intent to address crossover issues and limit consultation overload, this approach posed a number of challenges for the AASB in seeking stakeholder input. These challenges included the following:

- **Discussions were often limited to certain key issues** - The length of the document and volume of issues made it challenging to engage stakeholders on all of the relevant issues in the ITC. This inevitably resulted in certain issues not being discussed with all of the applicable stakeholders; and
- **The depth of discussion of the possible actions for any one issue was limited** - During a particularly busy period for many of our stakeholders, they could only afford to commit limited time to this consultation. Given the volume of material and complexity of the document, in some cases the merits of all actions for any one issue could not be discussed in the desired depth.

In light of these challenges, the AASB cautions the IAASB in taking a similar approach on future projects. In the AASB's view, the challenges encountered in engaging with stakeholders on this ITC may have outweighed the benefits.

### Scalability and public interest considerations

The possible actions to enhance audit quality included in the ITC may be based primarily on comments received from regulatory bodies or users of the financial statements of global or multi-national companies. Many listed entities in Canada would be considered small or medium-sized from a global perspective. Certain of these actions may be unnecessarily complex in the context of a small audit environment and challenging to apply to audits of smaller entities in Canada.

In Canada, aside from listed entities and certain not-for-profit organizations, an audit is often not mandated or required by local statutory requirements. The AASB is already aware of a trend in recent years towards a reduction in the

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number of audit engagements, which are being replaced by review or compilation engagements. There is therefore an overall public interest concern that more prescriptive and complex standards could have a significant negative impact on the demand for audits and continued performance of them by small and medium practices (SMPs).

The AASB understands that the IAASB will use feedback obtained on this ITC to determine the direction of its projects, and consider implementing certain of the possible actions. In progressing to these next steps, it is important that the IAASB carefully consider how it responds to issues raised. The AASB noted several issues where changes to standards may not be the most appropriate response. The AASB believes that some issues may be better addressed by improvements in how the existing standards are operationalized. The IAASB should make changes to standards only when there is compelling evidence that a standards change is in fact needed.

It is important that the IAASB assess whether proposed actions would result in a sufficient change in audit quality to justify the likely costs to be incurred. While audit quality is important, and undoubtedly in the public interest, so too is a thriving and sustainable audit profession.

#### The desire to balance the needs of all stakeholders

The AASB noted several possible actions proposed where the objective of those actions appear to be focused on reducing or eliminating inspection findings. While reducing inspection findings is a laudable goal, the AASB has seen situations where inspection findings relate more to the implementation of the standard, than to deficiencies in the standard itself. In the AASB's view, the IAASB's role in enhancing audit quality should not be overly driven by a desire to address inspection findings through new requirements without evidence of a deficiency in the requirements as a source of inspection findings. The AASB should seek to balance the issues and suggestions raised by all of its key stakeholders in a principles-based manner. The IAASB is therefore encouraged to determine, and communicate clearly, how the actions it takes appropriately respond to the views of all of the IAASB's stakeholders. This is what ultimately will drive substantive improvements in audit quality.

#### The role of other stakeholders in enhancing audit quality

There are many stakeholders who have a role in enhancing audit quality. As the role of standard setting can be limited in its reach, it is important that the appropriate stakeholders are engaged to assist in achieving an overall enhancement to audit quality. The majority of the possible actions proposed within the ITC are focused on changes to the ISAs, impacting the practitioner's audit approach. However, the AASB, as well as many of our Canadian stakeholders, recognize that there is a role for others in enhancing audit

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quality. For example, management has a role through ensuring the preparation of timely and sound financial information. Audit committees also have a role, through their governance and oversight of management and the practitioner. The IAASB is therefore encouraged to consider whether an appropriate action in response to the issues may be to engage and, where possible, attempt to influence these groups' support of audit quality.

### **Overall comments on key topics**

#### Professional scepticism

Professional skepticism is the cornerstone of an audit. Although certain of our Canadian stakeholders indicated that they believe the practitioner's application of professional skepticism is robust, the AASB believes that further improvements can be made. Canadian regulators continue to identify a lack of appropriate application of professional skepticism as a root cause in their inspection findings, in particular in highly complex areas such as ISA 540<sup>1</sup>. Therefore, the AASB is supportive of the IAASB's efforts in the challenging but critical area of professional skepticism.

The AASB does however caution the IAASB as actions to enhance the application of professional skepticism are pursued, that the need for auditing standards to continue to allow for audits to be conducted efficiently and economically is kept top of mind. For example, if an increased emphasis is placed on the practitioner seeking contradictory evidence with an attitude of presumptive doubt, the AASB, in addition to certain of our Canadian stakeholders, expressed concern that this will inappropriately raise the amount of evidence practitioners must obtain to constitute sufficient appropriate audit evidence. Given the inherent judgment involved in applying professional skepticism, it is important that the IAASB give appropriate guidance to ensure that the possible actions pursued maintain an appropriate balance of the costs and benefits.

Overall, it was clear to the AASB through our stakeholder consultations that the IAASB should focus their immediate efforts on:

- ensuring consistency in how professional skepticism is described throughout all the relevant international standards; and
- including guidance throughout the ISAs on how to appropriately demonstrate and document its application.

Efforts to make changes in these areas are expected to have a positive impact on ensuring consistency and enhancement of the application of professional skepticism in the audit.

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<sup>1</sup> ISA 540, *Auditing Accounting Estimates Including Fair Value Accounting Estimates, and Related Disclosures*

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### Quality control

The AASB is not convinced that there are deficiencies with ISQC 1<sup>2</sup> that require wholesale changes be made at this point in time. The AASB does support the IAASB revising or adding to application material as appropriate. In the AASB's view, of the three main topics in this ITC, the IAASB's focus should be on group audits and professional skepticism.

While some AASB members and our Canadian stakeholders were intrigued by the quality management approach (QMA) to redrafting ISQC 1, they commented on the lack of clarity about what it would look like in practice. Further, the IAASB also proposes a number of new or revised quality control requirements in the rest of the ITC. It is not clear how the inclusion of numerous requirements would fit into a risk-based QMA. For these reasons, the AASB and our Canadian stakeholders were unable to conclude on whether a QMA will enhance audit quality. The AASB recommends that if the IAASB receives sufficient support for moving forward with the QMA, it should study the approach further and more clearly articulate how firms would implement it, perhaps with examples. It would be especially useful for the IAASB to demonstrate what a quality control system prepared using a QMA would look like for firms of differing sizes and how it would be different from the current approach.

As noted earlier, scalability is a key concern. SMPs in Canada can struggle in applying ISQC 1. The main cause of these challenges is often cited as being a lack of availability of resources. Smaller firms often do not have enough personnel to appropriately segregate duties to allow independent persons to conduct these processes. Outsourcing is possible in some markets, but problematic in smaller communities. Accordingly, the AASB encourages the IAASB to be particularly cognizant of the challenges facing SMPs in considering changes to ISQC 1, and two areas in particular – engagement quality control review and monitoring.

### Group audits

The AASB is highly supportive of the IAASB's initiative to amend ISA 600<sup>3</sup> and provide guidance related to group audits. During consultations, our Canadian stakeholders expressed support for this initiative and exhorted the IAASB to act quickly. Auditors have struggled in understanding and implementing key sections of this standard. In addition to large accounting firms in Canada, CPA Canada has developed various guidance material for group audits since the

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<sup>2</sup> ISQC 1, *Quality Control for Firms that Perform Audits and Reviews of Financial Statements, and Other Assurance and Related Services Engagements*

<sup>3</sup> ISA 600, *Special Considerations – Audits of Group Financial Statements (Including the Work of Component Auditors)*

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implementation of ISA 600. The AASB believes building clarity and guidance into the standard will lead to greater consistency in application and improve audit quality.

The AASB supports a top-down risk based approach, as scoping a group audit based on the identification of components (bottom-up approach) may not always result in an appropriate assessment of the risks of material misstatement at the group financial statement level. In making changes to requirements and application material in ISA 600, the IAASB should be mindful of maintaining appropriate flexibility within the standard to allow for the application of this approach. For example, when making explicit reference to principles in ISAs 315<sup>4</sup> and 330<sup>5</sup>, the guidance should highlight the starting point is the risk assessment at the group level followed by drilling down to significant components (and their significant risks). An alternative bottom-up approach of performing the initial risk assessment at the component level could result in the identification of component risks that are not relevant to the group. Further, when responding to risks of material misstatement, any changes to requirements for work effort at significant and non-significant components should be premised on the work required to support the group audit opinion. Concern has been raised that if work effort requirements are addressed at the component level in isolation, the requirements could inappropriately result in work being performed on individual components that have limited significance to the group audit opinion. Ensuring that changes to requirements and application material support the application of a top-down risk based approach in ISA 600 will further promote consistent application of the standard by auditors.

While some Canadian stakeholders believe the group audit standard needs to be more prescriptive, the AASB felt this approach would undermine the ability of the standard to be broadly applied. Due to the diversity in group structures and environments, it is vital that requirements remain principles-based so they can be applied to a broad range of circumstances. Although application material can offer further guidance and practical examples, it is not possible to address all group audit scenarios. Therefore, in developing enhancements to ISA 600, the AASB encourages the IAASB to maintain a principles-based approach where emphasis is placed on addressing key challenges.

### **Responses to the specific questions**

In the IAASB's ITC, a number of possible actions have been proposed to address the issues and challenges identified. In responding to the ITC questions in

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<sup>4</sup> ISA 315, *Identifying and Assessing the Risks of Material Misstatement Through Understanding the Entity and Its Environment*

<sup>5</sup> ISA 330, *The Auditor's Responses to Assessed Risks*

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certain of the attached appendices, the AASB has highlighted the actions we consider, in light of input received from our Canadian stakeholders, to be most meaningful, meaningful, or those we do not support. Although other possible actions in the ITC may not be highlighted in these appendices, they may be of some benefit. However the AASB chose to stress the actions that address key challenges faced by practitioners, or where gaps in the standards have been identified.

Please refer to the following appendices:

- **Appendix B:** General questions
- **Appendix C:** Professional skepticism
- **Appendix D:** Quality control
- **Appendix E:** Group audits

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We hope that these comments will be useful to the IAASB in determining the appropriate next steps relating to these key projects. If you have any questions or require additional information, please contact Eric Turner at (416) 204-3240.

Yours very truly,



Darrell Jensen CPA, CA  
Chair, Auditing and Assurance Standards Board (Canada)

c.c. Canadian Auditing and Assurance Standards Board members  
Ron Salole

## **APPENDIX A: Summary of AASB consultations on the IAASB's ITC**

### **Groups consulted**

#### Preparers

- Chartered Professional Accountants of Canada's (CPA Canada) Small Company Advisory Group, comprised of management/preparers of financial information for small public companies.
- CPA Canada's Strategy, Management Accounting & Finance Advisory Board, comprised of senior business and finance leaders from across Canada.

#### Investors

- The Canadian Accounting Standards Board's User Advisory Council, comprised of professionals representing a variety of investment and analytical disciplines.

#### Academics

- Ad-hoc group of five university professors specializing in audit and assurance from various universities across Canada.

#### Practitioners

- CPA Canada's Practitioners Technical Advisory Board, comprised of professionals in public practice working with private small or mid-market enterprises and not for profit organizations.
- Chartered Professional Accountants of Ontario's (CPA Ontario) Small-Medium Practice Advisory Committee, comprised of professionals in public practice working with small-market enterprises.
- Staff of the Canadian Council of Legislative Auditors.

#### Regulatory Bodies

- Staff of the Canadian Public Accountability Board.
- Staff of the Office of the Superintendent of Financial Institutions.
- Staff of the Canadian Securities Administrators.
- A group of practice inspectors from CPA Ontario.

#### Chartered Professional Accountants Provincial Bodies

- Chartered Professional Accountants of Saskatchewan.

### **Formal response letters received**

- One response letter from a provincial Chartered Professional Accountants body.
- Two response letters from large public accounting firms.

## APPENDIX B: Responses to General Questions

General Questions	
G1(a-b)	The AASB agreed that the public interest issues identified in Table 1 of the ITC were relevant to the work on these topics. Please refer to general comments provided in our response letter regarding additional public interest considerations.
G1(c)	<p>The AASB and our Canadian stakeholders agree that overall audit quality is not just dependent on standard setting by the IAASB. In particular, there is a role for audit committees, market regulators, and others, to influence audit quality.</p> <p>One Canadian stakeholder expressed the view that currently, many of these other stakeholders influence audit quality reactively, for example, by writing to national and/or international standard setting bodies regarding standard setting matters. In their view, these other stakeholders could take a more proactive approach to positively influence audit quality by engaging, encouraging and, to a lesser extent, regulating management to improve the quality of the financial information they produce and their internal accounting and control systems.</p> <p>The AASB believes such efforts of other stakeholders to take a more proactive approach to enhancing audit quality should be embraced and encouraged. These efforts combined with the work of the IAASB will allow for more significant progress to be made on many of the initiatives within this ITC.</p>
G2	<p>A number of our Canadian stakeholders indicated that a project to revise ISA 500<sup>6</sup> should be undertaken by the IAASB.</p> <p>One Canadian stakeholder expressed concerns as to whether ISA 500 still remains fit for purpose, given the current changes to business operations. In particular, given an increase in the use of information technology has changed sources of audit evidence. Further concerns were expressed by a number of our Canadian stakeholders that ISA 500 will need to be revised following the implementation of certain possible actions proposed in the professional skepticism section of the ITC.</p> <p>The IAASB could consider whether a broader revision to ISA 500 would be appropriate to coincide with the timing of these likely changes.</p>
G3	<p>During one of our Canadian stakeholder consultations, reference was made to the following paper which was published in 2013 relating to professional skepticism.</p> <p><i>Research on Auditor Professional Skepticism: Literature Synthesis and Opportunities for Future Research</i></p> <p>Authored by: R. Hathy Hurtt, Helen Brown-Liburd, Christine E. Early, and Ganesh Krishnamoorthy</p>

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ISA 500, *Audit Evidence*

This paper discusses professional skepticism based on the initial premise that a lack of skepticism in the audit can either be as a result of:

- A failure in problem recognition (lack of skeptical judgment); or
- A failure to act on a problem recognized (lack of skeptical actions).

In addition the following document published in the American Accounting Association journal – Auditing: A Journal of Practice & Theory in February 2016, Vol. 35, No.1, pp.65-88, was raised by the AASB as being relevant to this ITC:

*Waves of Global Standardization: Small Practitioners’ Resilience and Intra-Professional Fragmentation within the Accounting Profession*

Authored by: Sylvain Durocher, Yves Gendron, and Claire-France Picard

This paper examines how small practitioners perceive and react to global standards and the underlying mechanisms put in place by the accounting profession to ensure “appropriate” implementation. Of particular interest are the challenges faced by SMPs and the “constant monitoring gaze” being felt by SMPs.

Given the relevance of these documents to the topics included in the ITC, the IAASB may wish to consider them as progress continues on these projects.

## APPENDIX C: Responses to Professional Skepticism Questions

In the IAASB’s ITC, a number of possible actions have been proposed to address the issues and challenges identified. In this appendix, the AASB highlights the actions we consider, in light of input received from our Canadian stakeholders, to be most meaningful, meaningful, or those we do not support. Certain other possible actions not highlighted in this appendix may be of benefit. However the AASB chose to stress actions that address key challenges faced by practitioners, or where gaps in the standards have been identified.

Professional Skepticism	
PS1	<p>The AASB, in addition to a number of our Canadian stakeholders, were of the view that how professional skepticism is defined and referred to throughout the ISAs was consistent with their interpretation.</p> <p>One Canadian regulator however thought that the definition should be revisited. They were of the view that the definition should emphasize, to a greater extent, that the practitioner should have an underlying presumption of doubt when performing audit procedures.</p> <p>The AASB however did not agree with the regulator’s view. The extant definition of professional skepticism allows for guidance on the application of professional skepticism to be included within the individual standards and appropriately applied based on the associated risks being addressed. If the definition was modified towards an attitude of presumptive doubt, this may inappropriately raise the amount of evidence practitioners must obtain to constitute sufficient appropriate audit evidence for the entire audit.</p> <p>The AASB believes that the definition, as written, is not in itself flawed, and that the real challenge in practice is its application which can be better addressed through guidance. Therefore, the AASB recommends the following enhancements be made:</p> <ul style="list-style-type: none"> <li>• Include application guidance in each of the relevant ISAs on how professional skepticism can be demonstrated and documented, specifically within the context of the requirements of each standard. The IAASB could also consider whether non-authoritative guidance may be more suited for this purpose. Such guidance would provide an opportunity to further develop the concept of professional skepticism and its application, including examples, but allow for more limited changes to the standard.</li> <li>• Consider enhancing the definition itself to highlight the following additional points raised by our Canadian academic stakeholders: <ul style="list-style-type: none"> <li>○ Greater emphasis could be made to the fact it is a state of mind that is continuous and ongoing throughout the audit, not a consideration and conclusion reached at one specific point in time. For example, the diagram in the right margin of pg. 13 of the ITC implies that professional skepticism is applied in making professional judgments, but is only indirectly relevant to the documentation of professional judgments and related actions. Such a view, if taken to the extreme, would imply that auditors cannot document the application of professional skepticism, which is worthy of</li> </ul> </li> </ul>

	<p>debate.</p> <ul style="list-style-type: none"> <li>○ The definition lacks any discussion on how the practitioner needs to be skeptical of their own judgment/bias in addition to that of management (i.e., auditor bias). The IAASB could consider whether a more general reference to biases, both auditor and management, could be explicitly included in the definition.</li> </ul>
PS2	<p><b><u>Impediments</u></b></p> <p><u>Key impediments</u> identified by the AASB and our Canadian stakeholders were:</p> <ul style="list-style-type: none"> <li>● Personality traits and cognitive biases such as confirmation, overconfidence, anchoring and availability biases</li> <li>● Tight reporting deadlines</li> <li>● Heavy staff workloads</li> <li>● Fee pressures</li> <li>● Fear of audit tendering, in particular for large clients that represent significant revenue for the audit firm</li> <li>● Perceived conflicting priorities between enhancing <u>audit</u> quality vs. enhancing <u>service</u> quality</li> <li>● Engagement team dynamics – individual skepticism may be negatively influenced by the level of skepticism of others on the engagement team (groupthink)</li> <li>● Lack of experience with audit engagements, which may be the case with some SMPs whose practice has a very limited number of audits</li> <li>● Firms having staff focus primarily on the steps and procedures in the audit, without appropriate time spent teaching the fundamental concepts. Such behaviour often is thought to drive a checklist mentality when approaching the audit.</li> </ul> <p>In many of our stakeholder discussions, there was lengthy debate as to whether a long-term client relationship is a driver or an impediment to the application of professional skepticism.</p> <p>Some of our Canadian stakeholders were of the view that these long term relationships impede the application of professional skepticism, given the practitioner may be unduly influenced by historical experience and assume all risks are low and/or rely too heavily on management’s explanations. Other of our Canadian stakeholders were of the view that long-term client relationships enhance professional skepticism through a thorough understanding of the client’s business and their industry. Only when you have sufficient knowledge and expertise can you be appropriately skeptical of management’s actions and financial results.</p> <p>The AASB agrees with the differing views expressed by the various stakeholders, and is of the view that this is an area where guidance and application material may be beneficial. For example, guidance outlining potential safeguards to enhance the application of professional skepticism in situations where the client relationship may be relatively new, or in existence for a lengthy time, could be considered during the client acceptance/continuance stage of the audit.</p>

**Drivers**

Key drivers identified by the AASB and our Canadian stakeholders were:

- Personality traits – for example, certain individuals have greater fortitude to challenge management
- Engagement team knowledge and competence and access to resources
- Tone at the top set by the engagement partner, or in the case of a firm, audit leadership of the firm
- Effective performance of an EQC review, when one is required
- Competent audit committee members who ask appropriate questions of the management and of the practitioner
- For the public sector – the expectation of the auditor is to identify reportable findings

**Role of IAASB**

The AASB and our Canadian stakeholders struggled with identifying ways in which many of the impediments/drivers could be addressed/enhanced through actions of the IAASB. With the exception of a few areas, there is a limited role for standard setting. Consequently, the AASB is of the view that the IAASB's key role is to encourage the application of professional skepticism throughout the standards in light of these challenges.

The AASB therefore recommends that the IAASB consider:

- Including examples of common impediments, within application guidance in the standards, to remind the practitioner as to the presence of these challenges. This may help encourage the application of professional skepticism in light of these impediments.
- Enhancing the application of professional skepticism when determining the appropriate direction of EQC reviews (part of the quality control section of the ITC).
- Including additional discussion in ISQC 1 regarding tone at the top, specifically relating to professional skepticism, such as a requirement for periodic training or professional development to reinforce common impediments and the importance of the issue.

Please refer to our response to PS3 for recommendations on how the areas discussed in paragraph 37 should be prioritized.

PS3	<p>The AASB and our Canadian stakeholders believe the following actions would be:</p> <p><b>Most meaningful:</b></p> <ul style="list-style-type: none"> <li>• <b>Ensure the concept of professional skepticism is consistently described across the International Standards (para. 37, 1<sup>st</sup> bullet)</b> – This was identified by the AASB as well as our Canadian stakeholders as a key first step in this project. Ensuring consistency across these standards is necessary in order to provide better clarity to the understanding of the concept by practitioners.</li> <li>• <b>Application guidance on how to demonstrate and document the application of professional skepticism throughout the specific ISA sections (para. 37, 2<sup>nd</sup> bullet)</b> – As discussed in our response to PS1, the AASB is of the view that this would be the most meaningful action that could be undertaken by the IAASB. This would also include ensuring the use of appropriate terminology and language. The AASB and our Canadian stakeholders believe that this is the single biggest challenge currently faced by practitioners.</li> <li>• <b>Importance of incorporating professional skepticism into ISA 540 (and other standards) (para. 39)</b> – Similarly to the point above, it was clear from our consultations with our Canadian stakeholders that, although practitioners may understand what professional skepticism is, the key struggle is its application when fulfilling the requirements of each of the ISAs. Given this issue, in addition to the application guidance noted above, further detail as to how to apply professional skepticism needs to be incorporated into the requirements throughout the ISAs, in particular ISA 240<sup>7</sup>, 315, 500, 540, 600 and ISQC 1. These standards deal with a critical stage of the audit in ensuring the appropriate application of professional skepticism. Further explanation on how to apply professional skepticism within these standards themselves will be key to making significant improvements.</li> </ul> <p><b>Meaningful:</b></p> <ul style="list-style-type: none"> <li>• <b>Determining how auditors can be effectively trained and their competencies further developed to enhance the application of professional skepticism (para. 37, 4<sup>th</sup> bullet)</b> – Many of our Canadian stakeholders were of the view that professional skepticism is a mindset, and that there is a key role for education in enhancing its application. Therefore, the AASB believes it would be beneficial for the joint working group to consider whether enhancements to training and development of the practitioner’s competencies could assist in encouraging the application of professional skepticism in the audit.</li> <li>• <b>Consider the potential effect of the evolving use of technology in audits and increasing business complexity, including information gathering about</b></li> </ul>
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ISA 240, *The Auditor’s Responsibilities Relating to Fraud in an Audit of Financial Statements*.

	<p><b>the use of audit data analytics (para. 37, 7<sup>th</sup> bullet and para. 40(a))</b> – Given the changes in how audits are being performed and in particular the increased trend towards data analytics in the audit, this is an area which would be meaningful for the IAASB to consider. Certain of our Canadian stakeholders raised concerns that the automation of the audit and use of checklists and templates is negatively impacting the application of professional skepticism today. Conversely, one of our Canadian stakeholders was of the view that the trend towards automating the audit and use of data analytics may assist with the application of professional skepticism by addressing certain of the impediments including certain auditor biases. Further research and guidance into this area to provide better clarity as to the appropriate view is therefore required.</p> <ul style="list-style-type: none"> <li>• <b>Reviewing the role of engagement partners, EQC reviewers, audit committees, audit oversight bodies and others in influencing the appropriate application of professional skepticism (para. 38 (a)(i))</b> – The importance of “tone at the top” was a key theme throughout many of our Canadian stakeholder interactions. In particular, we heard a consistent view from management/preparers that the partner’s involvement in the audit has a direct and noticeable impact on the application of professional skepticism. Therefore, reviewing the role of engagement partners in influencing the application of professional skepticism is a meaningful action. Similarly, the importance of the EQC review was expressed by certain of our Canadian stakeholders and shared by the AASB. Finally, the effectiveness in the oversight by audit committees of management and of the work performed by the practitioner can have a positive impact on the application of professional skepticism. The AASB recognizes the challenges often faced by the IAASB in influencing change in audit committees; however any efforts in this area would be beneficial.</li> <li>• <b>Reinforce that quality is essential in performing audits and highlight the importance of internal culture (para. 37, 8<sup>th</sup> bullet)</b> – The AASB recognizes the importance of internal culture in enhancing the application of professional skepticism. Our consultations with our Canadian academics raised the issue of team dynamics on the audit engagement and how groupthink can have a significant effect on the application of professional skepticism. This is an area where limited focus has been placed when considering impediments to the application of professional skepticism. The joint working group’s efforts to emphasize quality in performing audits and highlight the importance of internal culture may have a positive effect on these challenges.</li> </ul> <p><b>Not supported:</b></p> <ul style="list-style-type: none"> <li>• <b>Determining how International Standards should recognize and address the nature of the auditor’s personality traits and biases (para. 37, 5<sup>th</sup> bullet)</b> – While the AASB acknowledges that biases could be more appropriately addressed in the ISAs (refer to PS1), the AASB is of the view that recognizing and addressing the nature of the practitioner’s personality</li> </ul>
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	<p>traits is beyond the scope of standard setting and, in particular, the role of the IAASB. The AASB understands the challenges that personality traits can bring to the application of professional skepticism; however believes that this action may be more suitably considered by the International Accounting Education Standards Board (IAESB) as an area which would benefit from additional training. Such training could recognize the challenges that certain personality traits present, and educate practitioners on how to appropriate apply professional skepticism in light of those challenges.</p> <p><b>More information is needed:</b></p> <ul style="list-style-type: none"> <li>• <b>Development of a professional skepticism or professional judgment framework (para. 37, final bullet)</b> – The AASB as well as our Canadian stakeholders were unable to conclude whether development of a framework would be meaningful. We believe that more information is needed to understand what would be included in the framework, and how it would be used, in order to determine whether the AASB would be supportive this action.</li> </ul>
PS4	Refer to response in PS2 and PS3.
PS5	<p>The AASB and our Canadian stakeholders acknowledge the challenges expected for the IAASB in addressing this important topic area. In particular, difficulties, given the fact that many of the impediments to professional skepticism are actions which the IAASB is unable to influence directly. Given these challenges, the AASB is supportive of the IAASB’s collaboration with the International Ethics Standards Board of Accountants (IESBA) and IAESB, in addition to others. To be successful, certain of these groups have a role to play in carrying out many of the possible actions supported by the AASB.</p>

## APPENDIX D: Responses to Quality Control Questions

In the IAASB’s ITC, a number of possible actions have been proposed to address the issues and challenges identified. In this appendix, the AASB highlights the actions we consider, in light of input received from our Canadian stakeholders, to be most meaningful, meaningful, or those we do not support. Certain other possible actions not highlighted in this appendix may be of benefit. However the AASB chose to stress actions that address key challenges faced by practitioners, or where gaps in the standards have been identified.

<b>Quality Management Approach</b>	
QC1(a)	<p>While some AASB members and our Canadian stakeholders were intrigued by the previously defined QMA to redrafting ISQC 1, they commented on the lack of clarity about what it would look like in practice. Further, the IAASB also proposes a number of new or revised quality control requirements in the rest of the ITC. It is not clear how the inclusion of numerous requirements would fit into a risk-based QMA. For these reasons, the AASB and our Canadian stakeholders were unable to conclude on whether a QMA would enhance audit quality. The AASB recommends that if the IAASB receives sufficient support for moving forward with the QMA, it should study the approach further and more clearly articulate how firms would implement it, perhaps with examples. It would be especially useful for the IAASB to demonstrate what a quality control system prepared using a QMA would look like for firms of differing sizes and how it would differ from one prepared using ISQC 1.</p> <p>Comments supporting a QMA include:</p> <ul style="list-style-type: none"> <li>• There may be benefits to taking a proactive approach to quality. Revisiting quality control policies and procedures under a QMA may provide the opportunity to identify efficiencies in the audit approach.</li> <li>• Since auditors take a risk-based approach to conducting audits, it would not be difficult to extend this approach to their quality control system.</li> <li>• As risks are likely to change over time, firms will be required to more regularly update their quality control policies and procedures.</li> </ul> <p>Comments against a QMA include:</p> <ul style="list-style-type: none"> <li>• The IAASB seems to be endorsing the QMA and also proposes a number of new or revised requirements relating to quality control. It is not clear how the inclusion of numerous requirements fit into a risk-based approach.</li> <li>• The ITC does not describe a QMA in enough detail to understand how it would be made operational. This makes it difficult to assess whether the potential benefits will be realized. Some Canadian stakeholders indicated they could not support the QMA without a clearer understanding of how QMA could be applied by smaller firms.</li> <li>• There is a view that changing ISQC 1 to a QMA will only result in a more bureaucratic quality control process. Firms will have to invest resources to document the process that could be better focused on more meaningful improvements to audit quality. The cost to implement could be significant,</li> </ul>

	particularly for SMPs, and would likely exceed the benefits.
QC1(b)	No additional elements were identified. As noted above, it would be useful to see a sample system of quality control prepared using a QMA. It may then be easier to identify any additional elements to be included.
QC1(c)	It is not clear whether changes to ISQC 1 would affect the ISAs. However, given the close link between ISQC 1 and ISA 220 <sup>8</sup> , the IAASB should ensure that it reviews ISA 220 at the same time as ISQC 1. Without seeing the proposed revisions to ISQC 1 or what a QMA might look like, it is not possible to comment on possible revisions to ISA 220 or other ISAs.
QC1(d)	As noted in the overall comments, the AASB does not see a strong need to make significant revisions to the requirements in ISQC 1. The AASB believes that the IAASB has higher priority projects that it should focus on before embarking on a major revision to ISQC 1. However, if the IAASB decides to proceed with a project to revise ISQC 1, the matters described in Table 2 could be addressed. The AASB and Canadian stakeholders note that scalability is likely the most important of the areas noted in Table 2.
<b>Engagement Partner Roles and Responsibilities</b>	
QC2(a)	<p>The AASB and our Canadian stakeholders believe the following actions would be:</p> <p><b>Meaningful:</b></p> <ul style="list-style-type: none"> <li>• <b>Active involvement of the engagement partner in the risk assessment, planning, supervision and review of the work performed (para. 85, 2<sup>nd</sup> bullet)</b></li> <li>• <b>More proactive, scalable and robust approach to the identification of risks to audit quality at the engagement level (para. 85, 3<sup>rd</sup> bullet)</b></li> <li>• <b>Consider the need to develop requirements or application material to specifically address situations where the engagement partner is not located where the majority of the audit work is performed (para. 85, last bullet)</b></li> </ul> <p>These areas are critical to audit quality, therefore, it is important to focus on these to enhance clarity and consistency of application. The AASB and our Canadian stakeholders believe that additional requirements are likely not necessary. Additional application material should be sufficient to address these actions. The AASB notes that the partner’s role should not differ simply because the partner is not located there the majority of the audit work is performed: the audit partner is equally responsible for direction, supervision and review for all audits. Some stakeholder views were expressed that the last bullet noted above should also be dealt with in ISA</p>

<sup>8</sup> ISA 220, *Quality Control for an Audit of Financial Statements*

	<p>600 (see Appendix E, GA1).</p> <p><b>Not supported:</b></p> <ul style="list-style-type: none"> <li>• <b>Strengthening requirements and application material to clarify what is meant by performance, direction, supervision and review by the engagement partner (para. 85, 1st bullet)</b> – ISQC 1, paragraphs 32 and A32-A35, sufficiently addresses what is meant by performance, direction, supervision and review. The AASB and our Canadian stakeholders do not believe that more material is necessary. Nothing has been brought to our attention to make us believe that there is inconsistent application, or misunderstanding, of the existing requirements and application material.</li> <li>• <b>Acknowledging situations relating to the signing of the auditor’s report in the ISAs (para. 86)</b></li> <li>• <b>Clarifying the expected performance requirements for individuals other than engagement partners who sign or who are named in the auditor’s report (para. 86)</b></li> </ul> <p>The AASB, and several Canadian stakeholders, believe that proposed actions related to signing the auditor’s report proposed in the ITC are outside the scope of ISQC 1 (see also QC2(b) below). Further, views were expressed that these proposed changes would not serve to improve audit quality.</p>
QC2(b)	<p>The situations in which an individual other than the engagement partner signs the auditor’s report can vary widely. As noted in the ITC, there may be situations where the engagement partner is temporarily unavailable when the auditor’s report needs to be signed, so another partner in the firm signs the report. A very different example, which is common in the public sector in Canada, is one where an auditor general contracts the work to support the opinion to a third party auditing firm while the auditor general signs the auditor’s report that is publicly available. Also, some jurisdictions require the audit opinion to be signed by a partner licensed to sign the auditor’s report in that jurisdiction even though the direction, supervision and review takes place in another jurisdiction. The involvement of the signing partner in the work of the other auditor is likely to vary significantly depending on the scenario. In some cases, the signing partner may be able to rely on the direction, supervision and review performed by the engagement partner. The AASB believes that this is an area that needs further consideration but may be difficult to address, because of the possible widely-varied scenarios.</p>
<b>Others Involved in the Audit</b>	
QC3(a)	<p>The AASB, along with our Canadian stakeholders, are not convinced that changes in this area are necessary. The proposed action to further consider issues and concerns</p>

	<p>relating to the involvement of auditor’s experts (para. 104) could be helpful, but is likely better addressed in a separate project to deal with ISA 620<sup>9</sup> rather than in ISQC 1.</p> <p>However, if the IAASB chooses to proceed with changes, the following actions would be:</p> <p><b>Meaningful:</b></p> <ul style="list-style-type: none"> <li>• <b>Incorporate matters such as assessment of professional competence and capabilities of other auditors and evaluation of the sufficiency and appropriateness of their work (para. 100)</b> – The AASB notes that standards already include requirements and application material related to competence of engagement team members and others (e.g., ISQC 1, paragraphs A18, A25-A26 and A40; ISA 220, paragraphs 14 and A11; ISA 620, paragraph 9, A3, A6, A9, A14-A17 and A32). Additional guidance may be useful to assist with consistency in practice, particularly since existing guidance is not summarized in one location in the standards.</li> </ul> <p><b>Not supported:</b></p> <ul style="list-style-type: none"> <li>• <b>Revisit requirements that preclude reference to the report of another auditor (para. 101)</b></li> <li>• <b>Explore the ability to use another auditor’s report as audit evidence (para. 101)</b></li> </ul> <p>These issues have been discussed several times in the past, most recently as part of the auditor reporting project. The IAASB has not presented any new information or evidence in support of this action that would change previous decisions. Further, the AASB believes that this is an auditor reporting issue, not a quality control issue, and therefore should not be addressed in ISQC 1</p>
QC3(b)	As noted above, the AASB believes that dealing with the issue of the involvement of others in an audit engagement would likely best be addressed under ISA 620.
<b>The Firm’s Role in Supporting Quality</b>	
QC4(a)	<p>The AASB and our Canadian stakeholders believe the following actions would be:</p> <p><b>Meaningful:</b></p> <ul style="list-style-type: none"> <li>• <b>More explicitly address the considerations about the extent to which firms can rely on network quality control and monitoring policies and procedures in designing policies and procedures (para. 114(a))</b></li> <li>• <b>Strengthen requirements and application material relating to inspections that have taken place across the network (para. 114(b))</b></li> </ul> <p>It would be meaningful to address these areas, although changes could likely be limited to revisions to, or addition, of application material rather</p>

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ISA 620, *Using the Work of an Auditor's Expert*

	<p>than to requirements. Such changes could serve to improve clarity and consistency and close an expectations gap. However, the AASB is concerned that this could be difficult to achieve, as firms may not be permitted or willing to share such information across the network.</p> <p><b>Not supported:</b></p> <ul style="list-style-type: none"> <li>• <b>Consider whether requirements should be established for networks (para. 116)</b> - The AASB and several Canadian stakeholders believe that the IAASB should not attempt to establish requirements for networks. Due to the nature of networks, this would be difficult to achieve. The ITC sets out reasons why it would be difficult in paragraph 116; we agree with these reasons.</li> <li>• <b>Providing requirements or application material to more explicitly address direction, supervision and review of procedures performed at a centralized location or by other centralized resources (para. 123)</b> – The AASB notes that ISQC 1 applies regardless of whether the firm uses ADMs or not. Roles, responsibilities and audit documentation should be the same, regardless of where or how audit procedures are performed. The AASB does not see an urgent need for additional material in ISQC 1 to deal with this topic. A Canadian regulator did express the view that the role of the engagement partner should be clarified when ADMs are used. However, this stakeholder also noted that it does not have significant concerns in this area: ADMs do not appear to be widely used, or when they are used, they seem to be more commonly used for lower risk areas of the audit.</li> </ul>
QC4(b)	As noted above, the AASB does not believe that ISQC 1 should include requirements or application material to include networks. However requirements or application material to address how a firm should deal with inspections that have taken place across the network would be useful.
<b>Governance of the Firm, Including Leadership Responsibilities for Quality</b>	
QC5(a)	<p>In the AASB’s view it would be meaningful to incorporate commonly used and familiar terminology (para. 132). Such changes could serve to improve consistency across the profession.</p> <p>However the AASB did not support the remaining proposed actions. From the AASB’s point of view, it is not clear whether ISQC 1 is deficient in this area. In addition, the proposals appear to be very prescriptive in nature. It is not clear how such level of prescription would be achieved if a QMA to the standard is taken. Finally, the AASB expressed concern about the IAASB going beyond its mandate in this area.</p>
QC5(b)(i)	No, as noted above

QC5(b)(ii)	The AASB felt that ISQC 1 should not address accountability of firm leadership, or appropriate personnel within firm leadership, for matters related to quality, including independence-related matters. In many firms, this is already done in practice. In others, particularly in smaller firms, it would be difficult for firms to achieve. The AASB feels that the IAASB’s proposals should be scalable, and does not believe that this suggestion is scalable.
QC5(b)(iii)	As noted in QC1, views of Canadian stakeholders on the QMA are split. Without greater detail about a system of quality control prepared using a QMA, it is difficult to comment on whether the use of a QMA would provide better support or context for quality-related responsibilities for firm leadership and related accountability
<b>Engagement Quality Control (EQC) Reviews and Engagement Quality Control Reviewers (EQCR)</b>	
QC6(a)	<p>The EQC review is an area that provides significant practical challenges for SMPs in Canada. It can be difficult for SMPs, particularly those in smaller communities to find someone capable of performing the EQC review. The AASB and Canadian stakeholders ask the IAASB to address scalability when it considers actions related to the EQC review and EQCR. For example, the IAASB should carefully consider the implications for SMPs of any proposed revisions, in particular requirements to mandate EQC reviews beyond listed entities, and requirements related to the selection of the EQCR.</p> <p>In the AASB’s view the following actions would be:</p> <p><b>Most meaningful:</b></p> <ul style="list-style-type: none"> <li>• <b>Clarify the role of the EQCR in relation to the engagement partner (para. 145)</b> – It is critical to clearly define the roles. This action will address concerns that the role of the EQCR, in some cases, is seen as equal to that of the engagement partner. Some Canadian stakeholders expressed the view that changes in this area could drive a necessary change in behaviour and improve the consistency and effectiveness of EQC reviews.</li> </ul> <p><b>Meaningful:</b></p> <ul style="list-style-type: none"> <li>• <b>Expanding requirements to have an EQC review beyond audits of listed entities (para. 143, 1<sup>st</sup> bullet)</b> – The AASB and several Canadian stakeholders believe that changes to the requirements in this area are not required to change practice. What would be more beneficial is additional application material to explain the requirements in paragraphs 35(b) and (c). This is an area that is not well understood and has resulted in inconsistencies in practice. In addition, a Canadian regulator noted that documentation of what the EQCR reviewed could be improved.</li> <li>• <b>Strengthen requirements and application material regarding selection of the EQCR (para. 143, 2<sup>nd</sup> bullet)</b></li> <li>• <b>Strengthen documentation requirements to include timing and substance of the EQC review performed (para. 143, 3<sup>rd</sup> bullet)</b></li> </ul>

	<ul style="list-style-type: none"> <li>• <b>Strengthen requirements and application material by further specifying the nature and extent of matters to be considered by the EQCR (para. 143, 5<sup>th</sup> bullet)</b></li> </ul> <p>The AASB and our Canadian stakeholders were largely supportive of the above proposals, but noted that scalability for SMPs will likely be a challenge.</p> <p><b>Not supported:</b></p> <ul style="list-style-type: none"> <li>• <b>Disclosure in the auditor’s report if the engagement was subject to an EQC review (para. 144, 2<sup>nd</sup> bullet)</b> – Such disclosure is not seen as adding relevant information to the auditor’s report. The EQC review is only one aspect of quality control. Canadian investors noted that disclosure would only be useful if the findings were also disclosed. The AASB does not believe that this is feasible. During an audit, many issues may be identified, not only by the EQCR, but also by other members of the engagement team. Such issues are dealt with prior to the issuance of the audit report. To include such information in the audit report could cause confusion or be misinterpreted.</li> </ul>
QC6(b)(i)	<p>In general, the AASB and Canadian stakeholders have the view that the EQC review should be done based on risk, not mandated. ISQC 1, paragraph 35(b) requires firms to establish criteria against which assurance engagements other than audits of listed entities shall be evaluated to determine whether an EQC review should be performed. As noted above, many Canadian stakeholders are already performing EQC reviews on higher risk audits. There is limited application material in paragraph A41 therefore the requirement is open to interpretation. As a result some entities may be subject to EQC review, while others are not, although the risk may be the same for both. It may be appropriate to include additional application material to clarify how engagements may be selected for review.</p> <p>There may be potential consequences or other challenges if an EQC review is mandated for entities other than listed entities. For example, many small to mid-size not-for-profit entities in Canada are audited do not require an EQC review, because they are low risk. Should the IAASB mandate EQC review for audits of entities of particular public interest other than listed entities, the cost of such audits could increase significantly with little perceived benefit.</p>
QC6(b)(ii)	No. The subject of rotation is dealt with in the IFAC Code of Ethics.
QC6(b)(iii)	<p>The AASB and Canadian stakeholders did not arrive at a consensus conclusion on the issue of a separate EQC review standard.</p> <p>Comments supporting a separate standard include:</p> <ul style="list-style-type: none"> <li>• It will be clearer and may assist in understanding of the role of the EQC review.</li> <li>• In a separate standard, it may be easier to define what constitutes a “quality” audit and set out guidance on the minimum expectations for both the</li> </ul>

	<p>engagement partner and the EQCR.</p> <ul style="list-style-type: none"> <li>• A separate standard could more clearly set out what constitutes a risky engagement and, therefore, when an EQC review would be required.</li> </ul> <p>Comments against a separate standard include:</p> <ul style="list-style-type: none"> <li>• Sufficient revisions can be made within ISQC 1 to clarify the role of the EQC review.</li> <li>• The lack of a separate standard currently does not pose a high risk.</li> <li>• Having a separate standard may be misinterpreted by some as elevating the role of the engagement quality control review to a higher status than warranted.</li> <li>• The current standard is not overly lengthy; there is no need to bifurcate.</li> </ul> <p>These pros and cons are similar to those identified by the IAASB in the ITC. No new arguments, either in support of or against, have been brought to the AASB’s attention.</p>
<b>Monitoring and Remediation</b>	
QC7(a)	<p>Monitoring is an area that provides a significant challenge for SMPs in Canada. It can be difficult for smaller firms, particularly those in smaller communities to find someone capable of performing the monitoring function. The AASB and Canadian stakeholders ask the IAASB to address scalability when it considers actions related to monitoring. For example, revisions should not result in overly prescriptive requirements that are difficult for SMPs to apply. Further the amount of monitoring (i.e., the number of files subject to monitoring or the frequency of monitoring) should not be increased significantly.</p> <p>In the AASB’s view the following actions would be:</p> <p><b>Most meaningful:</b></p> <ul style="list-style-type: none"> <li>• <b>Require obtaining an understanding of causal factors of audit deficiencies (para. 157(a))</b></li> <li>• <b>Clarify necessary actions regarding analysis of audit deficiencies and corrective measures as a preventive measure (para. 157(b))</b></li> <li>• <b>Monitoring by firm leadership of the effectiveness and appropriateness of remedial actions (para. 158)</b></li> </ul> <p>It is always important to consider the causal factors so that corrective actions can be put in place. The AASB, along with many Canadian stakeholders, noted that some firms are already considering and addressing the causal factors. Conducting causal analysis is an integral part of a plan to improve audit quality. However, some Canadian stakeholders cautioned the IAASB to be careful to not increase the documentation requirements significantly as this would create an unnecessary burden on SMPs. Another Canadian stakeholder suggested that the IAASB’s focus should be on creating requirements or application material that emphasize the need to leverage or learn from existing inspections, rather than requiring additional</p>

	<p>inspections.</p> <p>Many firms, particularly larger firms, have an internal monitoring process in place that requires engagement partners to consider and respond to the results of the monitoring. Canadian stakeholders noted that it would be good to require firms to have a similar process in place to for external monitoring, and therefore support the IAASB’s proposals in this area.</p> <p><b>Meaningful:</b></p> <ul style="list-style-type: none"> <li>• <b>Strengthen requirements/application material on analysis of external findings (para. 156, 1<sup>st</sup> bullet)</b></li> <li>• <b>Consider whether inspection findings have implications on other engagements and the firm’s system of quality control (para. 156, 2<sup>nd</sup> bullet)</b></li> </ul> <p>Including requirements and application material in ISQC 1 could help improve consistency in practice. Further, consideration of external findings is seen to be of great benefit to firms. When firms consider the broader impact of findings on their practice, it is possible to make more wide-spread improvements.</p> <p><b>Not supported:</b></p> <ul style="list-style-type: none"> <li>• <b>Use of QMA to provide a stronger monitoring and remediation link (para. 159)</b> – As noted in the covering letter and response to QC1, the AASB and Canadian stakeholders are not convinced that ISQC 1 should be redrafted using a QMA. The IAASB states that the use of a QMA would create an opportunity to provide a stronger link to monitoring and remediation within the firm’s system of quality control. As the QMA has not been sufficiently articulated in the ITC, the AASB cannot conclude whether the IAASB’s statement is accurate.</li> </ul>
QC7(b)	<p>The AASB is supportive, for the reasons noted in QC7(a).</p> <p>Potential consequences or other challenges may include creating a compliance mindset, where practitioners are more focused on the process (i.e., completing a checklist) than on the purpose of such monitoring and remediation. Any revisions to ISQC 1 should be done in a manner that shines a positive light on monitoring, with the end result being that practitioners and firms consider whether audits have been done with the proper focus.</p>
<b>Engagement Partner Performance and Reward Systems</b>	
QC8(a)	<p>The AASB and some of its Canadian stakeholders do not support the proposals in this area. It is not within the mandate of audit standard-setters to prescribe a firm’s governing policies on these topics. If any changes are made to ISQC 1, they should be limited to application material. This would provide flexibility for firms to develop the best approach to comply with the standards. There are many factors that affect</p>

	engagement quality (for example, the quality of the accounting records), some of which are out of the control of the engagement partner. Compensation should not be linked to factors which are out of the individual's control.
QC8(b)	The AASB believes that the IAASB should take no action on this topic, for the reasons noted in QC8(a) above.
<b>Human Resources and Engagement Partner Competency</b>	
QC9 (a)-(b)	The AASB does not support the proposals in this area. Certain aspects of a firm's human resources function are already addressed in ISQC 1, paragraphs 29-31 and A24-A31. We believe that the aspects of human resources addressed in the ITC are largely outside the IAASB's mandate.
<b>Transparency Reporting</b>	
QC10(a)	<p>The majority of Canadian stakeholders, including users of auditor's reports, were not convinced that transparency reporting provides additional value. Transparency reports may be seen as being a marketing tool for firms rather than a tool to enhance audit quality.</p> <p>Two Canadian stakeholders felt that transparency reports could be useful. One noted that financial statement users may find the information in a transparency report useful when selecting an audit firm. Another noted that reports similar to transparency reports are issued in the public sector. This stakeholder felt that, if prepared with audit quality in mind, these reports could have a significant impact on audit quality. If firms have a responsibility to publicly report how they manage audit quality, they may be more likely to perform high quality audits.</p> <p>The AASB believes that the IAASB could monitor and facilitate ongoing dialogue on the topic of transparency, but should focus on other priority projects first. The AASB is not convinced that the IAASB needs to take an active role at this time. Rather, the IAASB should encourage other groups to first conduct research into the need for guidance, if any, on transparency reporting.</p>
QC10(b)	The AASB supports monitoring and facilitating ongoing dialogue and encouraging others to do research as noted in QC10(a). The AASB believes that any work on transparency reporting should take a lower priority until there is more broad public support for the concept of transparency reporting. The IAASB should not divert resources away from these projects to issue guidance or develop a thought piece or other non-authoritative material on transparency reporting at this time.
<b>Overall questions</b>	
QC11	As previously noted, the AASB does not believe that wholesale changes to ISQC 1 are required. However in reviewing the ITC, the AASB believes the list of quality control issues identified is very thorough. No other matters have come to our attention from Canadian stakeholders.

QC12	The AASB and Canadian stakeholders have not identified other specific actions that others could take in relation to quality control.
QC13	Considerations specific to SMPs have been noted in our answers above.
QC14	During our consultations, Canadian public sector practitioners noted that requirements based on criteria of being publicly accountable or of particular public interest may be problematic in the context of the public sector. Almost all of the engagements completed in the public sector could be captured by this terminology.

## APPENDIX E: Responses to Group Audit Questions

In the IAASB's ITC, a number of possible actions have been proposed to address the issues and challenges identified. In this appendix, the AASB highlights the actions we consider, in light of input received from our Canadian stakeholders, to be most meaningful, meaningful, or those we do not support. Certain other possible actions not highlighted in this appendix may be of benefit. However the AASB chose to stress actions that address key challenges faced by practitioners, or where gaps in the standards have been identified.

<b>Strengthening and Clarifying How the ISAs apply in a Group Audit</b>	
GA1(a), (b) and (d)	<p>The AASB as well as our Canadian stakeholders were of the view that enhancements to ISA 600 are required to provide more guidance for practitioners and build consistency in practice. At the same time, the IAASB should retain the principles-based nature of the standard. By enhancing ISA 600, the IAASB can provide guidance directly to address issues and challenges identified by practitioners.</p> <p>ISA 600 currently requires the application of all relevant ISAs, however practitioners struggle with how to implement this in practice. More examples of how the ISAs can be applied in a group environment will assist practitioners. In particular, guidance on how ISAs 315 and 320<sup>10</sup> can be applied in a group environment should be added to ISA 600.</p> <p>The AASB also believes that the scope of ISA 600 needs to be clarified to distinguish more clearly between multi-location audits and group audits. In addition, the AASB believes that paragraph 2 of ISA 600 may need to be amended to reflect the result of the actions set out in paragraph 100 of the ITC in response to the discussion in paragraphs 76-77 and 96 of the ITC dealing with letterbox audits.</p> <p>The AASB believes that paragraphs 195-198 of the ITC appropriately identify key challenges auditors encounter in conducting group audits. No further actions were identified to address the issues highlighted in these paragraphs.</p>
GA1(c)	<p>The AASB does not support further exploring making reference to another auditor in an auditor's report. This issue was debated during amendments to the auditor reporting standards. The AASB is not aware of factors to suggest that this topic should be re-opened. Further a Canadian investor group indicated that adding this information to the auditor's report might be confusing for investors. This investor group supported the group engagement partner taking full responsibility for the engagement as a whole. Reference to another auditor may imply divided responsibility.</p>

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ISA 320, *Materiality in Planning and Performing an Audit*

<b>Acceptance and Continuance of the Group Audit Engagement</b>	
GA2(a)	<p>The AASB and our Canadian stakeholders believe the following actions would be:</p> <p><b>Most meaningful:</b></p> <ul style="list-style-type: none"> <li>• <b>Strengthening the requirements in ISA 600: when not to accept the audit (para. 215(a))</b> – The AASB believes that earlier identification by the group auditor is important to bring to light when the preconditions of an audit are not present, particularly if the group auditor will not have access to the information or persons necessary in obtaining sufficient appropriate audit evidence.</li> </ul> <p><b>Meaningful:</b></p> <ul style="list-style-type: none"> <li>• <b>Strengthening requirements for understanding of group / components / environment (para. 217)</b> – The AASB supports this action in combination with the action in paragraph 215(b) below. The AASB believes understanding the group and the environment is vital to the risk assessment process. Emphasizing the need for professional skepticism when obtaining this understanding may also enhance better decision making around engagement acceptance and continuance.</li> <li>• <b>Clarifying the existing application material in paragraphs A10-A12 (para. 215(b))</b> – See also our comments on paragraph 217. When practitioners are dealing with foreign jurisdictions, it may be especially important to understand the impact of business, regulatory and cultural differences. More guidance in this area will help practitioners assess implications of these differences on the audit.</li> <li>• <b>More examples of access issues (para. 215(e))</b> – Providing more examples will help practitioners to understand what conditions should be considered when accepting a client and how those conditions may impact access to information. In particular, one Canadian stakeholder highlighted the need for guidance where the component is an investment accounted for by the equity method or is otherwise not controlled by the group and group management has little or no control to access component financial information. Further guidance for group auditors would be beneficial in this group scenario.</li> </ul> <p><b>Not supported:</b></p> <ul style="list-style-type: none"> <li>• <b>Strengthening the link in ISA 600 to ISQC 1 (para. 215(c))</b> – The AASB does not believe this action will change current behavior because paragraphs 4 and 19(b) of ISA 600 already appropriately address the need to consider the competence and capabilities of the engagement team.</li> </ul>

GA2(b)	<p>The AASB and our Canadian stakeholders believe access issues as described in paragraph 208(a) do occur and therefore further guidance would be useful.</p> <p>One of our Canadian regulators raised the concern that access is still an issue especially where the group engagement team is not authorized to do audit work in a foreign jurisdiction and therefore a component auditor needs to be engaged. Additional guidance on whether to accept this type of engagement and the pre-conditions that should be evaluated before acceptance of this engagement should be added to ISA 600. This stakeholder believes this particular access issue was not adequately discussed in the ITC and should be included in this project.</p> <p>Another Canadian stakeholder raised the issue of equity invested components. Without access to the component or their auditor, the only financial information available is the audited financial statements and auditor’s opinion. ISA 600 should provide guidance on how the audit opinion on the stand-alone financial statements can be appropriately used as audit evidence in these situations. See also our comment on paragraph 215(e) above.</p>
<b>Communications between the Group Engagement Team and Component Auditors</b>	
GA3	<p>The AASB and our Canadian stakeholders believe the following actions would be:</p> <p><b>Meaningful:</b></p> <ul style="list-style-type: none"> <li>• <b>Strengthening the requirements and application material in ISA 600 regarding instructions to component auditor (para. 224(a))</b> – The AASB believes greater emphasis on two-way communication throughout the audit will help to identify and address issues earlier in the engagement. ISA 600 provides some guidance and examples of sample communications with component auditors (Appendix 4: Examples of a Component Auditor's Confirmations and Appendix 5: Required and Additional Matters Included in the Group Engagement Team's Letter of Instruction). However some Canadian stakeholders have requested more guidance on what should be part of the reporting package and the level of detail in the instructions for component auditors. Currently, there is significant variation in the instructions provided to component auditors. Further examples can show considerations for the instructions and how to tailor requests based on the group structure and environment. Finally, it is important that requirements and application material continue to emphasize the importance of component auditors applying professional skepticism when performing procedures for the group auditor even though they do not have full responsibility for the group audit.</li> <li>• <b>Adding application material to strengthen documentation of significant communications (para. 224(d))</b> – Canadian regulators have noted a lack of audit evidence to support discussions of significant matters with component auditors in their inspection findings. The AASB believes that guidance on how to better apply ISA 230<sup>11</sup> (particularly paragraph 8) to documentation of significant communications between the group engagement team and component</li> </ul>

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ISA 230, *Audit Documentation*

	<p>auditors may assist the group engagement team to better understand the results of the work done by the component auditor.</p> <p><b>Not supported:</b></p> <ul style="list-style-type: none"> <li>• <b>Develop a separate standard for component auditors (para. 224(b))</b> – The AASB believes developing a separate standard for component auditors could lead to more confusion because the component auditor would need to comply with this standard while also following the group engagement team instructions. A separate standard could also undermine the group auditor’s responsibility for the full engagement. Further, a standard for component auditors would need to address a broad range of audits, which may not be practical. Better communication between auditors is needed and other actions such as improved group instructions may be more effective in achieving that.</li> <li>• <b>Consider whether requirement 48 in ISA 600 needs to be revised (para. 224(e))</b> – The AASB does not believe this is necessary since they believe paragraph 48 is clear and that this situation is rare in practice.</li> </ul>
<b>Using the Work of the Component Auditors</b>	
GA4	<p>The AASB and our Canadian stakeholders believe the following actions would be:</p> <p><b>Meaningful:</b></p> <ul style="list-style-type: none"> <li>• <b>Strengthening ISA 600 to clarify nature, timing and extent of involvement in work of component auditors (para. 242(a))</b> – In Canada, the large accounting firms have developed significant guidance in this area to support consistent work effort. The AASB believes that there is a need for this type of guidance to be built into ISA 600. Some Canadian stakeholders have also expressed the need to consider defining the role and responsibilities of the group and component auditor and what would constitute sufficient evidence of direction, supervision, and analysis of the component auditor’s work.</li> <li>• <b>Strengthening ISA 600 to emphasize need for greater focus and professional skepticism (para. 242(b), 1<sup>st</sup> bullet)</b> – Canadian regulators have noted lack of professional skepticism as a deficiency during group audit inspection findings. The group engagement team needs further guidance addressing how to demonstrate skepticism when assessing the work of component auditors.</li> <li>• <b>Providing further examples in application material for varying levels of involvement (para. 242(c))</b> – Although paragraph A55 in ISA 600 discusses forms of involvement the group engagement team may have with the component auditor, it does not identify the conditions under which those levels of involvement may be appropriate. Some Canadian stakeholders have expressed the need for more guidance about when it may be appropriate to conduct site visits vs. review of component auditor’s work remotely. Providing factors to consider when determining the appropriate level of involvement will assist auditors to operationalize the requirements in ISA 600.</li> </ul>

	<p><b>Not supported:</b></p> <ul style="list-style-type: none"> <li>• <b>Strengthening the requirements in ISA 600 by requiring explicit determination about component auditors' work (para. 234(a))</b> – By reviewing the component auditor’s work and signing off on the audit opinion, the engagement partner is already concluding about the component auditor’s work. Therefore making it an explicit requirement will not change the outcome.</li> <li>• <b>Developing application material to emphasize need to understand quality control monitoring and external quality control reviews for component auditors (para. 234(f))</b> – The AASB believes practitioners will not have access to quality control review results. Internal or external quality reviews are not usually shared with group auditors (especially if outside of the network). Therefore, this action will be difficult to operationalize.</li> </ul> <p><b>Other consideration:</b></p> <p>The AASB would also raise the <i>quality</i> of the evidence and which country/ environment it is coming from as a consideration for using the work of component auditors. ISA 600 does not raise this as a consideration. Further guidance on this topic and how the evaluation of audit evidence may be impacted by the country of origin of the evidence could assist auditors in appropriately addressing these challenges when designing audit procedures.</p> <p>One Canadian stakeholder requested particular guidance for engagements where the group engagement team does not have access to the component auditor’s working papers due to regulatory (state secrecy) restrictions. Considerations for how to demonstrate the group engagement team’s evaluation of the component auditor’s work and support the audit findings would be helpful for this scenario.</p>
<b>Identifying and Assessing the Risks of Material Misstatement in a Group Audit</b>	
GA5	<p>The AASB and our Canadian stakeholders believe the following actions would be:</p> <p><b>Most meaningful:</b></p> <ul style="list-style-type: none"> <li>• <b>Providing additional examples for relevant aspects and principles in ISA 315 and 330 that may arise from a group audit (para. 253(a))</b> – ISA 600 does not contain any specific requirements for identifying significant risks in a group audit. These requirements are contained in ISA 315. Canadian stakeholders are requesting further guidance in ISA 600 on how to apply ISAs 315 and 330 in a group audit environment. Guidance such as the risk factors discussed in Appendix 3 of ISA 600 and how these may impact classification of and work to be conducted at components would assist auditors to understand the implications of risks on the group audit. In particular, there is a need for guidance on how auditors fulfil the requirement in ISA 330 paragraph 18 for a group audit engagement. Guidance on how auditors design and perform appropriate substantive procedures for each material class of transactions, account balance, and disclosure, on which components, and how to determine when sufficient work has been done, will assist auditors to fulfil these requirements. This should be a top priority of this project.</li> </ul>

	<p><b>Meaningful:</b></p> <ul style="list-style-type: none"> <li>• <b>Clarifying or adding requirements or application material to emphasize that significant risks identified at specific components be considered at group level also (para. 253(b))</b> – Risks identified by component auditors are addressed in the work conducted on the component but often are missed for further consideration for the group as a whole (or other components). If the risk is applicable to other components and not appropriately identified, then sufficient and appropriate audit evidence will not be obtained. By emphasizing consideration at the group level of significant risks identified at certain specific components, group auditors would better address and consider significant risks and their implications for the group as a whole.</li> </ul> <p><b>Other consideration:</b></p> <p>The AASB did not arrive at a conclusion on the issue of pervasive significant risks. Some members are of the opinion that the standard requires clarification of how to address pervasive significant risks. Others believe this is an application issue and therefore more guidance should be added on determining how much work is enough. The IAASB may wish to investigate this further to ensure any proposed actions address the root cause of the issue. The AASB suggests that the IAASB consider this issue if other stakeholders identify this as a significant concern.</p> <p>The AASB also noted that shared services was mentioned as an issue in paragraph 244(d) of the ITC, however it was not addressed in any of the possible actions. One Canadian stakeholder raised a concern with group auditors not understanding how to treat shared services (as a significant component, or with group internal controls) and therefore not understanding the appropriate level of work that should be conducted. This may be another area for further guidance.</p>
<p><b>Issues Relating to Component Materiality and Other Aspects of Materiality Relevant to Group Audits</b></p>	
GA6	<p>The AASB and our Canadian stakeholders believe the following actions would be:</p> <p><b>Most meaningful:</b></p> <ul style="list-style-type: none"> <li>• <b>More guidance about how concepts of component materiality and component performance materiality are expected to be applied (para. 261(a))</b> – The AASB believes there is a lack of understanding by auditors for how to calculate component materiality based on the group circumstances, which has led to significant variation in practice. Some Canadian stakeholders are requesting clarification in how to determine overall group materiality and individual component materiality in accordance with ISA 320. This topic should be a priority area during this project and the IAASB should not delay until a project on ISA 320 can be started. The AASB would also stress that any guidance developed should be comprehensive and link the principles in ISA 320 and how they may be applied to a group environment.</li> </ul>

	<p><b>Meaningful:</b></p> <ul style="list-style-type: none"> <li>• <b>How materiality is applied in situations when procedures other than audits of financial information are being performed (para. 261(b))</b> - Although no issues and concerns were raised regarding this area during our consultations, the AASB believes materiality as a whole needs to be addressed for group audits and therefore this would be a by-product of that work. As an example, this guidance could highlight how to use the principles in ISA 320 when considering how to determine materiality for audits of classes of transactions or account balances or when performing analytical procedures.</li> </ul> <p><b>Other consideration:</b></p> <p>The AASB also noted that the concept of aggregation risk was raised as an issue in paragraph 255 of the ITC, however it was not specifically addressed in any of the possible actions. Canadian regulators have also raised this issue and that auditors do not understand and apply the concept appropriately, which affects the work effort on the group financial statements. This is another area where further exploration of the issues may be required.</p>
<b>Responding to Identified Risks of Material Misstatement in a Group Audit</b>	
GA7	<p>The AASB and our Canadian stakeholders believe the following actions would be:</p> <p><b>Most meaningful:</b></p> <ul style="list-style-type: none"> <li>• <b>Clarifying the expected work effort related to analytical procedures at the group level for components that are not identified as significant (para. 272(b)(v))</b></li> <li>• <b>Strengthening the requirements for the group engagement team to consider what work needs to be performed on non-significant components (para. 279(a))</b></li> <li>• <b>Providing further guidance on how the group engagement team should determine which non-significant components would require procedures (para. 279(b))</b></li> </ul> <p>In accordance with a top-down risk based approach, when the auditor is assessing whether sufficient appropriate audit evidence has been obtained to support the audit opinion, the auditor may determine that further work is required. For determining the work effort related to non-significant components, the AASB supports revisiting and clarifying the requirements in ISA 600. The work effort related to non-significant components is one area where significant auditor judgment is required. Providing examples may assist auditors in applying the requirements with greater consistency. Paragraph A51 of ISA 600 outlines some factors to consider when selecting the non-significant components for additional procedures and the type of procedures, however it does not discuss how to determine when a sufficient number of non-significant components have been selected to meet the requirement in paragraph 29 of</p>

	<p>ISA 600.</p> <p>Canadian regulators have also noted in their inspection findings a lack of sufficient and appropriate audit procedures relative to the risk or size of the component. Clarifying the requirements for the type of work required for significant and non-significant components will assist auditors in understanding the types of procedures they can perform and under which circumstances. The AASB feels the above actions must be addressed together by assessing types of procedures, the level of work to be conducted and how to determine when sufficient audit evidence has been obtained.</p> <p><b>Meaningful:</b></p> <ul style="list-style-type: none"> <li>• <b>Revisit requirements for the type of work required for significant and non-significant components (para. 272(a))</b></li> <li>• <b>Clarifying how procedures referred to in para. 272(b)(iii) can be distinguished from agreed-upon procedures (para. 272(b)(iv))</b></li> <li>• <b>More clearly distinguishing between types of procedures that can be performed, under which circumstances. (para. 272(b)(iii))</b></li> </ul> <p>In addressing what work needs to be done for non-significant components (as in para. 279(a) and (b)), auditors will also need to assess work done on significant components. Using the top-down risk based approach, requirements for significant and non-significant components must be assessed together to ensure sufficient appropriate audit evidence is obtained to support the group audit opinion.</p> <p>The AASB also supports clarifying the difference in work effort between specified audit procedures, specified procedures and agreed upon procedures (ISRS 4400)<sup>12</sup>. Component auditors require clarity as to the level of judgment permitted in ISA 600 when performing procedures for group auditors (for example, procedures performed under ISRS 4400 currently do not permit the use of judgment). Also, some auditors believe there is lack of common understanding when directing component auditors to perform certain procedures. Further clarification of these terms and work effort will assist group auditors to provide clear instructions and receive appropriate responses from component auditors.</p> <p><b>Not supported:</b></p> <ul style="list-style-type: none"> <li>• <b>Challenging the role of reviews of component financial information and whether they provide appropriate audit evidence (para. 279(c))</b> – The AASB believes reviews can serve a purpose in providing audit evidence and that the role of reviews in a group audit should be maintained.</li> <li>• <b>New application material to address group engagement team’s responsibilities for the consolidation process (para. 288, 3rd bullet)</b> – No issues related to the consolidation process were raised by our Canadian stakeholders.</li> </ul>
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ISRS 4400, *Engagements to Perform Agreed-Upon Procedures Regarding Financial Information*

	Therefore the AASB does not believe this action is required.
<b>Review and Evaluation of the Work of Component Auditors by the Group Engagement Team</b>	
GA8	<p>The AASB and our Canadian stakeholders believe the following actions would be:</p> <p><b>Most meaningful:</b></p> <ul style="list-style-type: none"> <li>• <b>Strengthening the documentation requirements for importance of documenting significant judgments related to the findings of the component auditors (para. 303, 2nd bullet)</b> – The premise of the audit is to obtain sufficient and appropriate evidence to support the audit opinion. The AASB believes that, while this is happening, documentation can be enhanced in relation to the group auditor’s judgment regarding component auditor’s findings. Time constraints can cause auditors to overlook key decisions or judgments and leave a gap in the documentation. More guidance on what types of significant communications to document and how to document the group auditor’s evaluation of component findings will assist auditors in operationalizing the requirements.</li> </ul> <p><b>Meaningful:</b></p> <ul style="list-style-type: none"> <li>• <b>Strengthening the communication requirements to emphasize ongoing two-way dialogue (para. 303, 1st bullet)</b> – The AASB believes that, while group auditors may be engaged in regular communications with component auditors, it is often not well documented. On-going communication is vital to execution of an effective group audit. This could be highlighted by enhancing the requirements in ISA 600.</li> </ul>
<b>The Impact of New and Revised Auditing Standards</b>	
GA9	<p><b>Do you believe ISA 600 should add requirements or application material to address relevant considerations about group financial statement disclosures? (para. 304)</b></p> <p>Yes. The group engagement team should consider the impact of component financial statement information on the disclosures in the group financial statements. Once again, the requirements and application material should highlight how to take a top-down risk based approach to identifying and capturing the appropriate disclosures. Development of more material in ISA 600 will highlight the importance of this and how to apply it.</p> <p><b>Do you believe ISA 600 should revise requirements or application material to address communication of key audit matters by the group engagement team in the auditor's report? (para. 305)</b></p> <p>Yes. The audit report on the consolidated financial statements should address any key audit matters coming from a component auditor if the item is significant and has an impact on the group.</p>

<b>Overall Questions</b>	
GA10	The AASB believes the list of group audit issues identified in this ITC is very thorough. There was one issue raised by one of our Canadian stakeholders which is discussed under GA2 above. No other matters have come to our attention from our Canadian stakeholders.
GA11	During the consultation process with our Canadian stakeholders, the AASB noted that, at times, regulators have different interpretations of some key sections of ISA 600, which ultimately may result in an inspection finding. It is vital that this stakeholder group be engaged throughout this process and support the final standard that is developed. Having a consistent understanding of the revised standard is imperative to the regulators role in ensuring audit quality is achieved.
GA12	In Canada, SMPs are generally not involved with group audits, and therefore we received limited feedback from SMPs with specific concerns relating to group audits. One of our practitioner stakeholders who acts as a component auditor expressed support for a separate component auditor standard. However, the AASB believes if appropriate and sufficient guidance for component auditors is included in ISA 600, a separate standard is not necessary.
GA13	During our consultations, no special considerations by public sector practitioners were raised. The AASB is of the view that group audit challenges in the public sector are largely consistent with those faced by other practitioners. As changes to specific requirements and application material are contemplated by the IAASB, further consultation with public sector members can be conducted to seek input regarding specific changes.