



Australian Government
Auditing and Assurance Standards Board

Podium Level 14, 530 Collins Street
Melbourne VIC 3000 Australia
PO Box 204, Collins Street West
Melbourne VIC 8007

1 July 2019

Mr Willie Botha
Technical Director
International Auditing and Assurance Standards Board
International Federation of Accountants
529 5th Avenue, 6th Floor
New York, NY 10017 USA

Dear Willie,

AUASB Submission on the IAASB's Exposure Drafts for Quality Management at the Firm and Engagement Level, including Engagement Quality Reviews - Responses to Overall and General Questions

The Australian Auditing and Assurance Standards Board (AUASB) is pleased to submit our response on the IAASB's Exposure Drafts for Quality Management at the Firm and Engagement Level, including Engagement Quality Reviews.

The AUASB is a non-corporate Commonwealth entity of the Australian Government, responsible for developing, issuing and maintaining auditing and assurance standards in Australia. The AUASB's role and mandate extends to liaison with other standards setters and participation in global standard-setting initiatives, so we have a very strong interest in these IAASB Exposure Drafts and welcome the opportunity to comment.

In formulating our response to these proposed standards the AUASB sought input from its stakeholders in three principal ways:

1. From hosting a series of roundtable meetings with stakeholders in three large Australian cities. These roundtable meetings were attended by over 50 stakeholders representing a broad range of backgrounds, including assurance providers from a range of audit firms, professional accounting bodies, academics, those charged with governance and preparers of financial statements.
2. Through an open invitation to provide comments on the equivalent AUASB issued Exposure Drafts via the AUASB website.
3. Formal discussions and deliberations by AUASB members at recent AUASB meetings.

The AUASB supports the IAASB's objective to develop and maintain robust international standards that contributes to enhanced engagement quality and consistency of practice throughout the world, and strengthened public confidence in the global auditing and assurance profession. However, the AUASB notes with concern that the IAASB's Exposure Drafts for Quality Management at the Firm and Engagement Level, including Engagement Quality Reviews, all contain greater complexity and detail than the extant standards they are replacing. This makes the proposed standards more challenging for all auditors (especially those auditors of smaller and medium or less complex entities) to apply, and may result in increased costs with arguably no commensurate increase in the level of audit quality for auditors of all types of entities.

As the IAASB continues to revise these proposed quality management standards, the AUASB considers it is in the public interest for the IAASB to more clearly demonstrate and articulate the benefits of the proposed quality management approach in each of the proposed standards (ISQM 1, ISQM 2 and ISA 220), and explicitly weigh these against the costs of transition and application, as a means to support the successful implementation of the proposed standards once they are finalised.

Detailed responses to the Overall and General Questions questions on the key issues considered by the IAASB in developing the Exposure Drafts have been included in the Appendix to this letter. Additionally,

individual responses to the questions contained in each Exposure Draft have been submitted via the IAASB's website.

However, as part of our overall submission on the IAASB's Exposure Drafts for Quality Management there are a number of specific matters which the AUASB would highlight in our response:

Overall considerations

Implementation Period

The AUASB considers that a longer implementation period is required, perhaps even considering a staggered implementation approach across key components. For example, commencing first with the governance and leadership components as the foundation of a firm's System of Quality Management, followed by the other components in subsequent periods.

ISQM 1 is expected to require a significant amount of firms' resources to put into place a risk assessment process and update firms' methodologies for the other two quality management standards. Stakeholders expressed concern that an 18-month implementation period for some network firms will be particularly challenging as the network head office may be responsible for developing certain parts of the system of quality management, which will then need to be tailored by individual firms to address their specific facts and circumstances.

Additionally, the AUASB is concerned that there are already two additional exposure drafts currently being finalised by the IAASB (ISA 315 and ISRS 4400) on top of the three new or revised standards included in the suite of Quality Management standards. The AUASB considers that for firms to implement changes in respect of all five of these standards almost simultaneously may have an adverse impact on quality, so a longer implementation period for these standards may be in the public interest.

ISQM 1

Structure and Granularity of the Standard

The AUASB supports a quality management approach to ISQM 1, however the AUASB is not supportive of the overall standard in its current form.

The AUASB considers the proposed standard to be a hybrid of risk-based quality management requirements that retains a granular level of prescriptive requirement carried over from the extant ISQC 1 standard, which undermines the proper application of a risk-based approach.

The main theme expressed by Australian stakeholders throughout the AUASB's outreach on ISQM 1 was related to its size and level of granularity. All practitioners, large and small, were concerned with the cost and resources needed to develop a quality management framework in line with the proposed standard as currently drafted. The AUASB encourages the IAASB to refine its drafting approach to reduce the length and complexity of the proposed standard, as well as the other proposed Quality Management Standards being exposed concurrently – ED-ISQM 2 and ED-ISA 220.

The AUASB considers that a quality management approach to ISQM 1 drafted on the same basis as the proposed new drafting approach to ISA 315 (i.e. the requirements being the "what", and the application material, appendices and guidance constituting the "why" and "how") would facilitate a better risk-based approach that is scalable to the specific circumstances of a firm. This may help mitigate the potentially large cost and resourcing burden that the implementation of this proposed standard imposes on practitioners.

The AUASB particularly highlights to the IAASB that the large volume of application material, appendices and guidance in the proposed standard needs to be reconsidered. Whilst these examples being included in the proposed standard may assist with implementation, the AUASB suggests the IAASB review the underlying principles in the requirements to make them simpler and more straightforward, which should alleviate the need for many of the examples and illustrations being included in the application guidance and appendices.

Additionally, the AUASB considers that the risk assessment process as designed has the potential to be particularly onerous for practitioners when considering the overall number of prescribed quality objectives

required by the proposed standard. To further support a risk-based approach, the AUASB recommends the removal of pre-defined required responses to quality risks in the standard as the AUASB considers that firms should determine their own specific responses tailored to their specific risk circumstances.

Public Interest Benefits

The AUASB considers that it is in the public interest for the IAASB to more clearly demonstrate and articulate the benefits of the proposed quality management approach in ISQM 1, and explicitly weigh these against the costs of transition and implementation, as a means to support the successful implementation of the proposed standard once it is finalised.

Scope of Engagements Subject to Engagement Quality Review

The AUASB does not support the explicit requirement to include ‘significant public interest’ entities in the scope of engagements subject to an engagement quality review. The AUASB supports a risk-based approach to such a determination which is already required in the proposed standard, where a firm is required to determine whether an engagement quality review is an appropriate response to assessed engagement risks.

It is unclear whether the proposed standard would result in an expectation that an engagement quality review is performed on ALL charities and ALL public sector engagements as these entities will always have a large number and wide range of stakeholders. This may be an unintended consequence of the proposed drafting. Furthermore, the AUASB is concerned that ‘significant public interest’ entity cannot be defined consistently across jurisdictions and therefore ISQM 2 would not be applied consistently.

ISQM 2

Guidance regarding a “cooling-off” period should reside in the IESBA Code

The AUASB strongly recommends that all guidance relating to the independence and objectivity of the Engagement Quality Reviewer (EQR) should reside in the IESBA Code as it already addresses these matters. Specifically the inclusion of alternative guidance regarding “cooling-off” periods in ISQM 2 increases the risk of inconsistent application and increases complexity for practitioners who may need to consider two different sources when addressing this issue. The AUASB recommends that the application material in ISQM 2 relating to any “cooling-off” period of the (EQR) should be removed from this standard and a reference to the IESBA code instead be considered (if this application guidance is to be retained).

ISA 220

Inconsistency in the engagement team definition and application guidance between ISA 220 and ISQM 1

The AUASB raises a significant concern that the definition of engagement team may be interpreted differently due to the different application and explanatory material that applies to this definition in ISA 220 (paragraphs A16-A19) not being replicated in ISQM 1. The impact may be that engagement team members are interpreted differently when the different application and explanatory material in each proposed standard is applied. For example, an Engagement Quality Reviewer (EQR) may be considered to be excluded from the engagement team under the definition and application guidance in ISA 220, but included as part of the engagement team under the definition in ISQM 1.

Should you have any queries regarding this submission, please do not hesitate to contact me or the AUASB Technical Director, Matthew Zappulla (mzappulla@auasb.gov.au).

Yours sincerely,



Professor Roger Simnett AO
Chair

Overall Questions

Q1. Do you support the approach and rationale for the proposed implementation period of approximately 18 months after the approval of the three standards by the Public Interest Oversight Board? If not, what is an appropriate implementation period?

The AUASB considers that a longer implementation period is required, perhaps even considering a staggered implementation approach across key components. For example, commencing first with the governance and leadership components as the foundation of a firm's System of Quality Management, followed by the other components in subsequent periods.

ISQM 1 is expected to require a significant amount of firms' resources to put into place a risk assessment process and update firms' methodologies for the other two quality management standards. Stakeholders expressed concern that an 18-month implementation period for some network firms will be particularly challenging as the network head office may be responsible for developing certain parts of the system of quality management, which will then need to be tailored by individual firms to address their specific facts and circumstances.

Additionally, the AUASB is concerned that there are already two additional exposure drafts currently being finalised by the IAASB (ISA 315 and ISRS 4400) on top of the three new or revised standards included in the suite of Quality Management standards. The AUASB considers that for firms to implement changes in respect of all five of these standards almost simultaneously may have an adverse impact on quality, so a longer implementation period for these standards may be in the public interest.

Q2. In order to support implementation of the standards in accordance with the IAASB's proposed effective date, what implementation materials would be most helpful, in particular for SMPs?

As noted above, the AUASB does not support the IAASB's proposed implementation period. Nonetheless, general implementation material, such as FAQs and specific examples addressing scalability of the requirements, would be highly desirable regardless of the implementation period selected. The AUASB also strongly encourages the IAASB to develop examples and scenarios in its implementation material that demonstrate how the standards would work for a sole practitioner or 2-3 partner firm.

The AUASB requests that the IAASB Quality Management Task Forces focus on identifying and developing appropriate 'implementation' support activities prior to the final agreed implementation date of the proposed standards. Considering the complexity and breadth of the proposed Quality Management standards there is a need for support materials to be issued by the IAASB simultaneously with the release of a final standard and not wait until the 'post-implementation' phase which appears to have been the case with ISA 540.



General Questions

- Q3. *Developing Nations* – Recognizing that many developing nations have adopted or are in the process of adopting the International Standards, the IAASB invites respondents from these nations to comment on the proposals, in particular, on any foreseeable difficulties in applying it in a developing nation environment.**

We have no specific comments on this question.

- Q4. *Public Sector* – The IAASB welcomes input from the public sector auditors on how the proposed standards affect engagements in the public sector regarding whether there are potential concerns about the applicability of the proposals to the structure and governance arrangements of public sector auditors.**

The AUASB does not support the explicit requirement to include ‘significant public interest’ entities in the scope of engagements subject to an engagement quality review.

The AUASB notes that Public sector engagements encompass a large range of diverse organisations both in terms of the size of the organisation and the nature of their activities. The AUASB considers that absent a more robust definition or description of what is meant by “entities of significant public interest,” there may be a number of public sector engagements that become subject to an engagement quality (EQ) review where such a review is not warranted.

- Q5. *Translations* – Recognizing that many respondents may intend to translate the final ISQMs and ISA for adoption in their own environments, the IAASB welcomes comment on potential translation issues respondents may note in reviewing the proposed standards.**

We have no specific comments on this question.