

REF#737346

1 July 2019

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International Auditing and Assurance Standards Board (IAASB)

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Submitted electronically at www.iaasb.org and to WillieBotha@iaasb.org

Dear Sir

COMMENT LETTER ON THE IAASB'S EXPOSURE DRAFTS FOR QUALITY MANAGEMENT AT THE FIRM AND ENGAGEMENT LEVEL, INCLUDING ENGAGEMENT QUALITY REVIEWS

The South African Institute of Chartered Accountants (SAICA) is the home of chartered accountants in South Africa – we currently have over 44,000 members from various constituencies, including members in public practice ($\pm 30\%$), members in business ($\pm 49\%$), in the public sector ($\pm 4\%$), education ($\pm 2.0\%$) and other members ($\pm 15\%$). In meeting our objectives, our long-term professional interests are always in line with the public interest and responsible leadership. SAICA is currently the only professional accountancy organisation that has been accredited by the Audit Regulator in South Africa, the Independent Regulatory Board for Auditors (IRBA).

We welcome the opportunity to comment on the IAASB'S Exposure Drafts for Quality Management at the Firm and Engagement Level, including Engagement Quality Reviews (QM-EDs). We wish to express our appreciation for the work of the IAASB's Quality Control Task Forces (IAASB Task Force) in addressing the fundamental topic of quality management.

Accompanying this cover letter, please find the comments prepared by SAICA on the QM-EDs-Quality.

Please do not hesitate to contact Hayley Barker Hoogwerf (hayleyb@saica.co.za) should you wish to discuss any of our comments.

Yours sincerely

Signed electronically

Hayley Barker Hoogwerf

Acting Senior Executive, Assurance and Practice

SAICA'S Approach to Respond

1. With the pervasive effect that the IAASB's project on Quality Management will have on all practices utilising these standards, SAICA engaged with our members to encourage firms and practitioners to closely monitor the progress made and, in line with change management, be proactive in providing feedback to SAICA on any comments that they may have; even before the exposure drafts were officially issued for comment. To this end, SAICA established the SAICA Quality Control Reference Group (SAICA Reference Group) that met continuously throughout 2018 to study the IAASB's Issues Papers relating to Quality Management.
2. An internal Working Group studied and debated the QM-EDs and prepared initial thoughts and inputs pertaining to the questions posed.
3. SAICA participated in the IRBA Quality Control Task Group (IRBA Task Group) meeting where interested parties were invited to provide their views and comments in finalising the IRBA and SAICA comment letters. The IRBA Task Group comprised representatives from the IRBA, SAICA, academia and audit firms.
4. Included in this comment letter are the details of the discussions held by the SAICA Reference Group as well as the IRBA Task Group. The purpose of including such detail is not necessarily to provide a definitive conclusion on the matters noted but rather to point out areas of concern for further consideration by the IAASB Task Force.

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5. The SAICA comment letter is structured in the following sections:
 - A. Specific Questions
 - B. Editorial Comments on Proposed ISA 220 (Revised)

A. Specific Questions

- 1) Do you support the focus on the sufficient and appropriate involvement of the engagement partner (see particularly paragraphs 11–13 and 37 of ED-220), as part of taking overall responsibility for managing quality on the engagement? Does the proposed ISA appropriately reflect the role of other senior members of the engagement team, including other partners?

Response:

6. SAICA is satisfied with and supports the focus on the sufficient appropriate involvement of the engagement partner, as well as the fact that ED-220 appropriately reflects the role of other senior members of the engagement team, including other partners.
7. With respect to paragraph 11 and the requirement for the engagement partner to create an environment that emphasizes the firm's cultural values and behaviors, a question was raised around how the engagement partner demonstrates that this requirement has been complied with. An illustrative example or other implementation guidance in terms of what the IAASB foresees being included in the audit file to demonstrate this will be most helpful in providing clarity on this.
8. Paragraph 11 continues to state that the engagement partner shall be sufficiently and appropriately involved throughout the engagement such that the engagement partner has the basis for determining whether the *significant judgements* made and the appropriate conclusions reached are appropriate. Extant ISQC 1 also makes reference to significant judgements made by the engagement team and the conclusions reached in formulating the report. During our outreach activities, a practical concern was raised in that there are differing measures used in identifying significant judgements, which results in differing views in terms of what is meant by this. Measures used to determine significant judgements include the materiality of an account balance, class of transactions or disclosures or where significant audit risks have been identified.
9. The differing views in terms of areas of *significant judgement* create a particular challenge in the performance of the EQR. In line with the purpose of the EQR for the engagement quality reviewer to perform an objective evaluation of the *significant judgements* of the engagement team and the conclusions reached in formulating the report, the question is whether the engagement partner and engagement quality reviewer have to agree on what constitutes a significant judgement.
10. In answering this question, reference is made to paragraphs A29 and A30 of ED-ISMQ 2. In expanding on the requirement for the engagement quality reviewer to identify the areas involving significant judgements made by the engagement team¹, the aforementioned paragraphs make specific reference to the examples of significant judgements identified by the engagement partner as contained in ED-220. It therefore seeming logical to conclude that the significant judgements identified by the engagement partner and engagement quality reviewer should be similar, barring differences as a result of the exercise of professional judgement.

¹ ED-ISQM 2, para. 22(C)

11. In line with our suggestion included in Response Template: Proposed ISQM 2, SAICA suggests that a definition for the terms *significant matters* and *significant judgements* be included in both ED-ISQM 2 and ED-220.

2) Does ED-220 have appropriate linkages with the ISQMs? Do you support the requirements to follow the firm's policies and procedures and the material referring to when the engagement partner may depend on the firm's policies or procedures?

Response:

12. SAICA is satisfied that ED-220 has appropriate linkages with the ISQMs. We support the approach taken whereby ED-220 is intended to operate as part of the broader SOQM established at firm level in accordance with ED-ISQM 1. We welcome the application material that clarifies that the engagement partner may be able to depend on the firm's policies or procedures in certain instances.

13. One area that perhaps requires further attention relates to Monitoring and Remediation. ED-220 deals how results of firm monitoring activities are dealt with at engagement level², but it is not clear how results of monitoring activities at engagement level impact on the firm SOQM.

3) Do you support the material on the appropriate exercise of professional skepticism in managing quality at the engagement level? (See paragraph 7 and A27–A29 of ED-220)

Response:

14. Professional scepticism is a difficult subject because of the level of judgement involved. ED-220 only makes reference to professional scepticism in three places in the body of the standard, namely paragraphs 6, 7 and 12 and without the related application material, the concept of professional scepticism and the required application is open to different interpretations. SAICA is in support of the additional application material included in paragraphs A27 – A 29 of ED-220. This is the first time that we are seeing this type of guidance. This is seen as a positive addition that is welcomed as providing useful guidance.

15. In relation to the application material, paragraph A27 includes examples of impediments to professional scepticism that the engagement partner may need to address. A question around whether impediments that are specific requirements for the auditor to comply with was raised. For example, ISA 315 (Revised) requires the auditor to obtain an understanding of the entity and its environment so how can insufficient understanding of the entity and the environment be an impediment.

16. To this end, the two specific examples that are in question are:

- Insufficient emphasis on the importance of quality may undermine the exercise of professional skepticism by the engagement team;
- Insufficient understanding of the entity and its environment, its system of internal control, and the applicable financial reporting framework may constrain the ability of the engagement team to make appropriate judgements and an informed challenge of management's assertions.

17. In relation to the impediment that may undermine the exercise of professional scepticism, the impediment that we see is when the auditor, including the engagement partner and the engagement team is not aware of the areas that are more susceptible to bias and therefore does not place the sufficient emphasis on the importance of exercising professional scepticism.

18. In relation to obtaining a sufficient understanding of the entity and its environment, the impediment we see is the existence of a barrier to obtaining the required understanding.

² ED-220, para. 36

19. We recommend that these specific examples included in paragraph A27 be reworded in line with the suggestion in the paragraphs above to clarify the impediment.
20. To echo the concerns noted in the response to ED-ISQM 1, concerns have been noted in relation to how the engagement partner demonstrates compliance with ED-220. A specific area of concern that was noted relates to auditor biases, as included in paragraph A28 of ED-220. This paragraph provides examples of biases that may affect the auditor's judgement. SAICA sees this as a positive addition to the application material. During our outreach activities, there was general consensus that the focus should be on how the auditor actually considers and demonstrates how these have been overcome, as opposed to focusing on the documentation. However, concerns were noted around how the auditor demonstrates that these have been considered and overcome.
21. In line with the recommendation included in the ED-ISQM 1 response letter, it is SAICA's recommendation that the IAASB engage IFIAR and other audit regulators in understanding how they intend regulating compliance with the requirements of the QM-EDs. The IAASB can then use input obtained through this engagement to create an illustrative framework of what *good* documentation entails, in indicating the bear minimum that is expected to be documented on file.
22. SAICA welcomes the addition of the guidance contained in paragraph A29 on possible actions that the engagement partner may take to deal with impediments to the exercise of professional scepticism, A question that was noted in relation to this was around the difference between the following possible actions:
- Changing the composition of the engagement team assigned, for example involving more experienced staff in order to obtain greater skills or knowledge or specific expertise.
 - Involving more experienced members of the engagement team when dealing with members of management who are difficult or challenging to interact with.
23. It is our understanding that the first point addresses who the members of the engagement team should be. In line with this, it is suggested that the second bullet point should then talk to how the audit work is allocated among the members of the audit team that has been established in accordance with the preceding bullet.
- 4) Does ED-220 deal adequately with the modern auditing environment, including the use of different audit delivery models and technology?

Response:

24. SAICA is in agreement with the fact that ED-220 now recognises that engagement teams may be organised in a variety of ways including being located together or across different geographical locations or organized by the activity that they are performing. This is now more in line with the reality of how engagement teams are actually structured.
25. We would, however like to highlight our concern with the view expressed in the Explanatory Memorandum to ED-220, where it states that ED-220 also recognises that individuals who are involved in the audit engagement may not necessarily be *engaged or employed directly by the firm*³. It is questionable whether an individual will ever perform audit procedures on the engagement without some form of prior engagement between this individual and the firm.
26. In reading the definition of *engagement team* together with paragraph A16, it is our view that the standard could be clearer on the fact that partners, staff and other individuals who perform audit procedures on the engagement are either employed by the firm or otherwise engaged.

³ Explanatory Memorandum to ED-220, para.8

27. The definition of *engagement team* indicates that an auditor's *external* expert engaged by the firm is excluded from the engagement team. SAICA concluded that the reason for the exclusion was that an auditor's expert is covered by ISA 620. However, the definition of an auditor's expert contained in ISA 620 states that an auditor's expert may be either an auditor's internal expert or an auditor's external expert. We therefore question why the definition of engagement team included in ED-220 makes specific reference to an auditor's **external** expert only. This may create confusion around whether an auditor's internal expert forms part of the engagement team or is specifically excluded and covered by ISA 620.
28. The definition of an engagement team states that this includes any other individuals *who perform audit procedures on the engagement*. A debate around the meaning of this ensued; specifically, around what is meant by *performs audit procedures on the engagement*. An example of a personal assistant performing the administration function in obtaining bank confirmations formed the basis of this discussion.
29. In reading paragraph A16 of ED-220, we noted that reference is made to paragraph A10 of ISA 500, which talks broadly about audit procedures for obtaining audit evidence but it is still not clear to what extent an individual is considered to have performed audit procedures.
30. In relation to the growing role of technology in audits of financial statements, we note and welcome the guidance contained in paragraphs A56 – A58 but feel that the standard is light in providing guidance on the use of different audit delivery models and technology.
- 5) **Do you support the revised requirements and guidance on direction, supervision and review? (See paragraphs 27–31 and A68–A80 of ED-220)**

Response:

31. During our outreach activities, a question around the significant revisions made to the requirements on engagement performance was raised; specifically, whether the changes contained in paragraph 27 of ED-220 will result in achieving the objective of clarifying the engagement partner's responsibilities and if the expanded application guidance contained in A72-A76 and A79 was useful.
32. The addition was welcomed in terms of providing clarity in relation to the engagement partner's responsibilities. To address a situation where the engagement partner only performs a review on a completed audit file when it is possibly too late for the engagement team to revise the audit approach, we suggest that the IAASB may consider including a requirement for the engagement partner to review the planned approach to significant risk areas, as well as areas involving significant judgement prior to the commencement of the audit field work.
33. SAICA notes the inclusion of the stand back provision to ensure that the engagement partner is satisfied that quality management at the engagement level has provided reasonable assurance that quality has been achieved.
34. We are in support of the inclusion of the stand back provision and believe that this contributes to achieving the objective of the engagement partner taking overall responsibility for achieving audit quality. Often, the engagement partner gets so involved in the detail that they forget to step back and consider the bigger picture.
35. During our outreach activities, a debate around whether this requirement needs to be specifically included or whether the engagement partner currently considers these without there being a formal

requirement ensued. The response was that these points are not always considered by the engagement partner and it is foreseen that the specific inclusion of this requirement will go a long way in changing this behavior.

- 6) Does ED-220, together with the overarching documentation requirements in ISA 230, include sufficient requirements and guidance on documentation?

Response:

36. We are satisfied that ED-220, together with the overarching documentation requirements in ISA 230 provide sufficient requirements and guidance in relation to documentation.

- 7) Is ED-220 appropriately scalable to engagements of different sizes and complexity, including through the focus on the nature and circumstances of the engagement in the requirements?

Response:

37. Certain of the requirements contained in ED-220 may not be applicable to sole practitioners and other smaller SMPs; specifically, in relation to direction, supervision and review. For example, a sole practitioner may not have other members of the engagement team to supervise⁴ or have discussions with⁵. ED-220 is however not clear in indicating that certain of the requirements are only applicable as may be required based on the nature and circumstances of the firm and the related engagements. This is an area that we suggest be relooked at.

B. Editorial Comments on Proposed ISA 220 (Revised)

38. In terms of the definition of engagement team, specific reference is made to ISA 610 in the actual definition but the reference to ISA 620 is included in a footnote, resulting in ISA 610 featuring more prominently in the definition. This may create the impression that ISA 610 is more important than ISA 620. It is therefore suggested that they either include the reference to both ISA 610 and ISA 620 in the actual definition or include a footnote for both.
39. Application paragraph A10 states that the *relative balance* of the engagement partner's efforts to comply with the requirements of this ISA (i.e. *between* implementing the firm's responses and designing and implementing engagement-specific responses beyond those set forth in the firm's policies and procedures) may vary. The firm's responses as contained in ED-ISQM 1 are compulsory procedures; yet this sentence seems to imply that the engagement partner has a choice as to which firm's responses to implement, rather than the engagement partners actions being an incremental response to quality risks. It is suggested that the wording of this be updated as follows:

~~between~~ In addition to implementing the firm's responses, the engagement partner's effort to comply with the requirements of this ISA in designing and implementing additional engagement-specific responses may vary.

⁴ ED-220, para. 27

⁵ ED-220, para. 28