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Mr. Willie Botha
IAASB Technical Director
International Auditing and Assurance Standards Board

International Federation of Accountants
529 5th Avenue
New York 10017
USA

Re: IAASB Exposure Draft: *Proposed International Standard on Quality Management 2 - Engagement Quality Reviews*

Dear Mr. Botha,

Further to our covering letter, please find below the BDO International (BDO) comments in respect of the aforementioned standard (ED-ISQM 2).

ISQM 2 draft comments

- 1) Do you support a separate standard for engagement quality reviews? In particular, do you agree that ED-ISQM 1 should deal with the engagements for which an engagement quality review is to be performed, and ED-ISQM 2 should deal with the remaining aspects of engagement quality reviews?**

Yes, on balance, we are supportive of the IAASB's decision to carve out the remaining aspects of the engagement quality review into a separate ED-ISQM 2.

We have noted previously that separating the specific requirements attached to an engagement quality review could help to provide greater clarity to those individuals performing this specific role. We are also mindful of the public interest arguments that point to the differentiation in the role and the need for the review itself, being separated for greater clarity. We also note that there is an inevitable risk that providing a separate ISQM 2 on engagement quality reviews could send an inadvertent message about this particular type of firm-level response, which could in turn de-emphasise the value attached to other types of firm-level responses.

In our view, an individual performing the engagement quality reviewer role operates in the context of a firm's quality management eco-system. The need to appoint an engagement quality reviewer is, of itself, a firm-level response to an assessed quality risk. On that basis, it is sensible that firm-level decisions about when an engagement quality review is required should be outlined in ED-ISQM 1. Conversely, role-specific considerations associated with the facts and circumstances of a particular engagement (such as engagement quality review performance, documentation and determination of who should perform the role) are more appropriately documented in ED-ISQM 2.

We also note that consolidating the previous requirements in this new ED-ISQM 2 (including the requirements in extant ISA 220 (Revised)) emphasises that the engagement quality review is a firm-level activity undertaken by an individual who is acting on behalf of the firm, not the engagement team.

2) Are the linkages between the requirements for engagement quality reviews in ED-ISQM 1 and ED-ISQM 2 clear?

Yes, the linkages between both sets of requirements outlined in ED-ISQM 1 and ED-ISQM 2 are clear.

On reading the individual standards, we do find that there is sufficient clarity to differentiate and also link the purpose and context of ISQM 1 and ISQM 2. We note that in respect of ED-ISQM 2 paragraph A35 and ED-ISQM 1 paragraphs 67 and 68 there are references to the engagement level documentation requirements relating to ED-ISQM 2 and the more general documentation requirements relating to firm-level systems of quality management. In our view there is the potential for confusion as these are two distinct types of documentation the purposes of which are quite different.

Given the propensity for users to access individual standards separately, we would ask that the IAASB reconsider the types of definitions that have been included in ED-ISQM 2. There is extensive use of specific terms within ED-ISQM 2 (firms, engagement partner, engagement team) that are excluded from the definitions in ED-ISQM 2. Consistent with ED-ISQM 1, it would be helpful to users to include these definitions in ED-ISQM 2, so they can understand the standard in context.

Regarding the definitions in these standards, we suggest a revision to the definition of 'engagement team'. The current definition in ED-ISQM 1 and ISA 220 provides exclusions for external experts and individuals within the client's internal audit function who provide direct assistance. If the definition provides exclusions, we believe it should also state that the engagement team also excludes engagement quality reviewers. This point is included in ED-ISQM 2 paragraph 17, but we believe for consistency, it should also be added as another exclusion in the definition of engagement team.

3) Do you support the change from "engagement quality control review/reviewer" to "engagement quality review/reviewer?" Will there be any adverse consequences of changing the terminology in respondents' jurisdictions?

Yes, we support the elimination of the term 'control' in the context of ED-ISQM 2. In our response to ED-ISQM 1 we have set out our concerns related to the proposed changes in terminology - noting that this can lead to difficulties for different types of stakeholders, jurisdictions where professional standards have to be translated and those jurisdictions where requirements have to be enshrined in law.

Notwithstanding our overall concern, we do recognise the need to replace 'quality control' with the concept of 'quality management' within ED-ISQM 2 to ensure consistency.

- 4) Do you support the requirements for eligibility to be appointed as an engagement quality reviewer or an assistant to the engagement quality reviewer as described in paragraphs 16 and 17, respectively, of ED-ISQM 2?
- (a) What are your views on the need for the guidance in proposed ISQM 2 regarding a “cooling-off” period for that individual before being able to act as the engagement quality reviewer?
- (b) If you support such guidance, do you agree that it should be located in proposed ISQM 2 as opposed to the IESBA Code?

We support the requirements for eligibility to be appointed as an engagement quality reviewer or an assistant to the engagement quality reviewer as described in paragraphs 16 and 17. However we believe that it would be helpful to include a statement in paragraph A13 to clarify the ethical requirements that are relevant to the engagement quality reviewer (or assistants) since they are not engagement team members.

We also note that while ED-ISQM 2 highlights the importance of ‘objectivity’ for an engagement quality reviewer, it is not clear whether this also applies to the assistant engagement quality reviewer.

While we are supportive of the requirement in paragraph 16 that the firm shall establish policies that include limitations on the eligibility of an individual to be appointed as an engagement quality reviewer for an engagement on which the individual previously served as engagement partner, we note the following:

- We agree with the guidance in paragraph A5 on why a ‘cooling-off’ period is necessary, although using the term ‘not likely’ in the first sentence seems to leave an opening for not having a cooling-off period at all (which is confirmed in paragraph 28 of the ED-ISQM 2 Explanatory Memo). For engagements where an objective engagement quality review is considered necessary, we cannot envision a situation where it would be appropriate to have no cooling-off period. If the IAASB wants to allow this possibility, perhaps there should be wording in the application guidance that states that no cooling-off period would be extremely rare.
- The role of assistant engagement quality reviewers is intended to be used on specific occasions; some examples in application guidance or implementation support (perhaps by way of a Frequently Asked Question (FAQ) scenario) may be helpful for users.
- As use of the word ‘previously’ leaves the determination of the exact length of the cooling-off period up to the firm (for non-listed entity audits), this may be an area where the IAASB may want to consider providing clearer implementation materials for firms.

We support the rest of the guidance on the cooling-off period in paragraph A5, including the 2-year period for listed entities although we note that that there is a risk that the 2-year cooling-off period (which is similar to PCAOB AS 1220¹) within the application guidance will become a rule of thumb or may be seen as a presumptive requirement. Providing a cross-reference to applicable IESBA² paragraphs in the application guidance (or acknowledgment of local requirements) would also be helpful for firms.

¹ US Auditing Standard 1220: *Engagement Quality Review*

² International Ethics Standards Board for Accountants

Regarding the other eligibility criteria for engagement quality reviewers, we note that paragraph A6 defines competence but never defines capabilities. The IAASB should consider whether a short discussion of capabilities would be helpful.

5) **Do you agree with the requirements relating to the nature, timing and extent of the engagement quality reviewer’s procedures? Are the responsibilities of the engagement quality reviewer appropriate given the revised responsibilities of the engagement partner in proposed ISA 220 (Revised)?**

We agree with the requirements relating to the nature, timing and extent of the engagement quality reviewer’s procedures in ED-ISQM 2 paragraphs 22 and 23. However, we suggest adding the following wording in paragraph 23 to recognise that engagement quality reviewers are also concerned with adequacy of documentation (additional wording is bolded):

‘If the engagement quality reviewer has concerns that the significant judgments made by the engagement team, or the conclusions reached thereon, are not appropriate or are not appropriately documented, ...’

We also agree with the requirements in paragraph 21 as we believe these policies are necessary to fulfill the engagement quality review objectives.

We agree that the responsibilities of the engagement quality reviewer are mostly appropriate given the revised responsibilities of the engagement partner in proposed ISA 220 insofar as they relate to interactions with the engagement quality reviewer. We note that the proposed standard no longer requires the engagement quality reviewer to have a role in consideration of independence matters. In our view, the role of the engagement quality reviewer, combined with their interaction with the engagement team, could arguably provide a more objective standpoint in this regard.

However, ED-ISQM 2 does not provide application guidance on the responsibilities of a replacement engagement quality reviewer appointed during the engagement when the eligibility of the original engagement quality reviewer became impaired (paragraph 19).

Also, in order to further support the requirements in:

- Paragraph 22 (a), (i) and (ii) about the availability, provision, nature and timing of results of a firm’s monitoring and remediation findings, and
- Paragraph 22 (g) regarding what could conceivably be a wide variety of current practices regarding engagement quality reviewer review of the financial statements,

for both situations it would be helpful to have clarification about the nature, timing and extent of each aspect of the engagement quality reviewer role.

While we acknowledge the application guidance A32 which supports paragraph 22 (e), it would be helpful to link this guidance to the concept of the firm’s intellectual resources as per ED-ISQM 1.

- 6) **Do you agree that the engagement quality reviewer’s evaluation of the engagement team’s significant judgments includes evaluating the engagement team’s exercise of professional skepticism? Do you believe that ED-ISQM 2 should further address the exercise of professional skepticism by the engagement quality reviewer? If so, what suggestions do you have in that regard?**

We agree that the engagement quality reviewer’s evaluation of the engagement team’s significant judgments includes evaluating the engagement team’s exercise of professional skepticism and that it is inherent in the proposed requirements. While we believe that more guidance on applying professional skepticism and documenting it would be useful, whether in relation to the engagement team or the performance of engagement quality reviewer role, we do not believe that it should be embedded solely in ED-ISQM 2 but should be considered across the body of standards. We understand that IAASB, in conjunction with IESBA and IAESB, already has a separate project underway addressing professional skepticism from a behavioural perspective; this may result in further development of additional guidance when the project finishes.

The IAASB may also wish to consider whether:

- There is an opportunity to replicate in ED-ISQM 2 some of the content in ISA 220 (Revised), paragraphs A27-A29 by exploring potential threats to engagement quality reviewer professional skepticism (such as confidence bias in the competence and capabilities of an engagement team).
- For an engagement quality review of audits, there is a potential conflict between EU regulations and ED-ISQM 2 as the EU regulations focus on the statutory auditor or key audit partner and whether they would have arrived at the opinion and conclusions expressed in the auditor’s report, versus the seemingly ambiguous language in ED-ISQM 2 which lacks specific reference to reports and focuses instead on the team.

- 7) **Do you agree with the enhanced documentation requirements?**

Yes, we support the enhanced documentation requirements.

- 8) **Are the requirements for engagement quality reviews in ED-ISQM 2 scalable for firms of varying size and complexity? If not, what else can be done to improve scalability?**

Yes, we believe that the requirements, in combination with the related application guidance, provide sufficient scalability for firms of varying size and complexity. An area that could potentially be considered through provision of an FAQ may be when an engagement quality reviewer is reviewing an engagement partner who also happens to be senior member of a firm’s leadership team along with potential mechanisms for dealing with this situation.

If the intention of ED-ISQM 2 is to increase usage of engagement quality reviews, then this may lead to potential challenges about availability of engagement quality reviewers in certain firms as well as a question about whether this is an appropriate safeguard in the case of non-audit engagements. For those firms who use external engagement quality reviewers, the expanded requirements also have the potential to impact audit quality by placing an even greater responsibility on firms to apply quality control processes to those external engagement quality reviewers to ensure they are competent and sufficiently familiar with the firm’s policies and procedures.

Other Comments on ED-ISQM 2

Effective Date

Paragraph 9 of ED-ISQM 2 suggests that there are two effective dates: one for audits and reviews of financial statements and a different one for other engagements. We do not understand why two different effective dates would be necessary. We assume the first effective date will be consistent with the effective date for ED-ISQM 1 and ED-ISA 220. If the entire system of quality management will be effective at that date, we see no reason to delay implementing ED-ISQM 2 for 'other engagement' types.

Other Minor Edits in ED-ISQM 2

We have also listed below some minor suggested edits for your consideration:

- Paragraph 10 - To improve linkage with ED-ISQM 1, we suggest adding the following words to the objective for ED-ISQM 2 (additional wording is bolded):

'The objective of the firm is to perform an engagement quality review for the engagement when an engagement quality review is required under ISQM 1.'

- Paragraph A4 - Consider replacing the references to network requirements in paragraphs 59 - 60 of ED-ISQM 1 with paragraph 58 - 63.
- Paragraph A4 - Consider replacing the references to service providers in paragraphs 65 of ED-ISQM 1 with paragraph 63 - 64.
- Paragraph A5 - Consider replacing 'immediate previous period' with 'immediately preceding period'.

We hope that our comments and suggestions will be helpful to you in your deliberations and finalisation of the suite of quality management standards.

Please contact me should you wish to discuss any of these comments.

Yours sincerely,

BDO International Limited

Chris Smith

Global Head of Audit and Accounting