ENGAGEMENT QUALITY REVIEWS—EXTRACT FROM PROPOSED ISQM 1 addressing engagements subject to an engagement quality review

(Marked from October 16, 2018 IAASB Teleconference)

Note to IESBA Meeting Participants – this extract is to be incorporated into reading of proposed ISQM 1 (Agenda Item 5-B). This contain paragraphs relating to requirements and application materials relating to engagement quality reviews.

Requirements

Engagement Performance

40. [Renumbered based on ISQM 1 renumbering] In designing and implementing responses to address the quality risks identified by the firm relating to the engagement performance quality objectives, the firm shall include the following responses:

... 

(e) Establishing policies or procedures addressing engagement quality reviews in accordance with ISQM 2, and that require an engagement quality review for: (Ref: Para. A102–A109)

(i) Audits of financial statements of listed entities;

(ii) Audits of financial statements of entities that the firm determines are of significant public interest; and

(iii) Audits or other engagements for which:

a. An engagement quality review is required by law or regulation; or

b. The firm determines that an engagement quality review is an appropriate response to assessed quality risks, based on the reasons for the assessments given to the quality risks.

...
Application Material

... 

Engagement Performance

[Deleted former para. A99 – points are generally addressed in the context of an EQR in paragraphs A11 and A12 of proposed ISQM 2. Other paragraphs renumbered based on ISQM 1 renumbering.]

Engagements Subject to an Engagement Quality Review (Ref: Para. 40(e))

A102. The categories of engagements for which an engagement quality review is required are not mutually exclusive. For example, many listed entities may be considered to be of significant public interest based on the characteristics described in paragraph A103. Similarly, the firm may conclude that an engagement quality review for an entity determined to be of significant public interest is also an appropriate response to an assessed quality risk. In addition, law or regulation may require engagement quality reviews to be performed for certain types of entities (e.g., entities with public accountability as defined in certain jurisdictions), or may include different criteria or characteristics that firms may use in determining whether an entity is of significant public interest.

A103. [Changed order of sentences] In determining whether an entity is of significant public interest, the firm may take into account, for example, the number and range of stakeholders and the nature and size of the business. The firm also may consider the relative significance of factors such as these in the context of the jurisdiction or region in which the entity operates. Entities that the firm determines to be of significant public interest may include entities such as financial institutions (e.g., certain banks, insurance companies, and pension funds), and other entities such as certain not-for-profit organizations.

A104. Law or regulation may require an engagement quality review to be performed, for example, for audit engagements for entities that:

- Are characterized as public interest entities;
- Operate in the public sector or which are recipients of government funding;
- Operate in certain industries (e.g., financial institutions such as banks, insurance companies and pension funds);
- Meet an asset threshold determined by law or regulation; or
- Are under the management of a court or judicial process (e.g., liquidation).

A105. Audits or other engagements for which the firm may determine that an engagement quality review is an appropriate response to assessed quality risks include, for example, engagements:

- That involve a high level of complexity or judgment, such as:
  - An audit of financial statements for an entity operating in an industry that typically has accounting estimates with a high degree of estimation uncertainty (e.g., certain large financial institutions or mining entities), or for which uncertainties exist related to events or conditions that may cast significant doubt on the entity’s ability to continue as a going concern.
An assurance engagement that involves difficulty by the practitioner in measuring or evaluating the underlying subject matter against the applicable criteria (e.g., a greenhouse gas statement in which there are significant uncertainties associated with the quantities reported therein).

- Where issues have been encountered on the engagement, for example, audit engagements with a history of identified misstatements or deficiencies in internal control, recurring internal or external inspection findings, or a material restatement of comparative information in the financial statements.
- For entities in emerging industries or that involve emerging technologies, or for which the firm has no previous experience.
- For which unusual circumstances are identified during the firm's acceptance and continuance of client relationships and specific engagements (e.g., a new client that had a disagreement with its previous auditor or assurance practitioner).
- That involve reporting on financial or non-financial information that is expected to be included in a regulatory filing, or that may involve a higher degree of judgment, such as pro forma financial information to be included in a prospectus.
- Engagements with negative findings arising from the firm's monitoring activities or external inspections, or engagements for entities for which concerns were expressed in communications from securities or prudential regulators.

[Former para. A102 moved to paragraph A96 of proposed ISQM 1 – see Agenda Item 2–A]

A106. In some cases, there may be no engagements for which an engagement quality review is required to be performed, or for which the firm would determine that an engagement quality review is an appropriate response to a quality risk (e.g., when a firm does not perform audits of listed entities or entities of significant public interest and other responses to assessed quality risks are determined by the firm to be appropriate).

Considerations Specific to Public Sector Audit Organizations

A107. Public sector entities may be of significant public interest due to the range of their stakeholders and the nature of the services they provide. Factors to consider in determining whether a public sector entity is of significant public interest may include whether the entity is a national, regional or local government, or whether an opinion is being expressed on the entire entity or only certain units.

A108. Other factors to consider may include whether the entity is a corporation that is state owned or in which the state has a controlling stake or a stake with significant influence. Larger public sector entities may be determined to be of significant public interest due to their social or economic influence on the community or region in which the entity operates.

A109. The firm may determine that an engagement quality review is an appropriate response to a quality risk for engagements in the public sector for which law or regulation establishes additional reporting requirements (e.g., a separate report on instances of non-compliance with law or regulation to the legislature or other governing body or communicating such instances in the auditor’s report on the financial statements).