



Office of the Auditor General of Canada
Bureau du vérificateur général du Canada

16 May 2016

International Auditing and Assurance Standards Board
545 Fifth Avenue, 14th Floor
New York, New York 10017
UNITED STATES OF AMERICA

RE: Invitation to Comment – Enhancing Audit Quality in the Public Interest

Dear Sir:

Thank you for the opportunity to comment on the above Invitation to Comment. I am responding on behalf of the Office of the Auditor General of Canada.

Our responses to the specific questions posed in the Invitation to Comment are provided below.

Sincerely,

Stuart Barr
Assistant Auditor General

Enclosure

cc. Eric Turner CPA, CA
Director, Auditing and Assurance Standards
Auditing and Assurance Standards Board

Professional Skepticism

1. Is your interpretation of the concept of professional skepticism consistent with how it is defined and referred to in the ISAs? If not, how could the concept be better described?

Our interpretation of the concept of professional skepticism is consistent with how it is defined and referred to in the ISAs. We hold the view that individual firms have a significant role to play in establishing and supporting a culture of appropriate skepticism and that training, coaching and supervision play a very important role in ensuring its application.

2. What do you believe are the drivers for, and impediments to, the appropriate application of professional skepticism? What role should we take to enhance those drivers and address those impediments? How should we prioritize the areas discussed in paragraph 37?

Within a public sector legislative audit office, professional skepticism may also be threatened by long tenure and inflexible cost structures. Legislative auditors with long tenure face familiarity threats that need to be actively managed in order to ensure professional skepticism is not put at risk. Further, a legislative audit office funded by parliamentary appropriations rather than client billings may benefit from increased independence, but will also face short-term pressures to contain audit effort to that originally budgeted in order to complete all statutory and discretionary engagements within available funding limitations. Short-term increases in audit effort may not be easily absorbed within authorized funding levels. This may negatively impact an auditor's willingness, capacity or perception as to the extent to which they may apply skepticism.

In our view, the above constraints and conditions are largely internal to the audit firm conducting the engagement and the appropriate response to these threats to professional skepticism rest primarily within the legislative audit office. Rotation and other strategies to manage familiarity risks should be in place to enable the appropriate application of professional skepticism. Firm level audit resource allocations should recognize that some engagements may require more resources than originally planned to address unanticipated issues including those arising from the application of professional skepticism. Firms must ensure budgets and related performance measures do not in fact or appearance unduly constrain the application of skepticism.

3. Is the listing of areas being explored in paragraph 38–40 complete? If not, what other areas should we or the Joint Working Group consider and why? What do you think are the most important area to be considered?

We have not identified other areas for the Joint Working Group to explore. We assessed the matter of risk assessment and the audit of management estimates as being the most important areas to be considered.

4. Do you believe the possible actions we might take in the context of our current projects relating to quality control and group audits will be effective in promoting improved application of professional skepticism? If not, why?

The possible actions described may be effective in improving the application of professional skepticism. Certain actions may be determined to warrant a higher prioritization based on consultation feedback.

5. What actions should others take to address the factors that inhibit the application of professional skepticism and the actions needed to mitigate them (e.g., the IAESB, the IESBA, other international standards setters or NSS, those charged with governance (including audit committee members), firms, or professional accountancy organizations)? Are there activities already completed or underway of which we and the Joint Working Group should be aware?

In our response to question 2, we have outlined the importance of firm/legislative auditor actions to enable and encourage the application of professional skepticism.

Quality Control

1. Use of a Quality Management Approach (QMA)

(a) Would use of a QMA help to improve audit quality? If not, why not? What challenges might there be in restructuring ISQC 1 to facilitate this approach?

The use of a QMA appears to be an opportunity to better integrate organizational risk management and audit quality risk management. The improved integration of the audit system of quality control and firm governance and risk management is a worthwhile exercise as currently, an audit system of quality control can operate in isolation or addition to the organization's overall risk management framework, particularly where the organization's mandate is broader than an audit practice. Further, a public sector legislative auditor may be subject to additional requirements (such as whistleblowing or other integrity provisions) that overlap but are not limited to audit engagements and that may not completely address requirements set out in audit standards such as ISQC 1. This may create duplication and complexity as the firm must implement policies and procedures that completely address a requirements of professional standards, law, regulation and public sector policy. Improved integration of risk management and monitoring would likely ultimately improve audit quality.

Challenges in restructuring ISQC 1 to facilitate a more risk based approach to audit quality include appropriately responding to the risk of inconsistent system design as each firm designs and implements policies and procedures relevant to the activities of the firm and its assessment of risk. The document for comment is unclear as to how the QMA would be scaled down for smaller firms/partnerships and sole proprietorships.

(b) If ISQC 1 is restructured to require the firm's use of a QMA, in light of the objective of a QMA and the possible elements described in paragraphs 64 and Table 3, are there other elements that should be included? If so, what are they?

We hold the view that a restructured ISQC 1 needs to continue to align to the elements found in best practice internal control frameworks such as the COSO framework.

If monitoring activities are recognized to include the results of external inspections, guidance as to whether these activities may reduce management monitoring activities should be provided.

(c) In your view, how might a change to restructure ISQC 1 impact the ISAs, including those addressing quality control at the engagement level?

Engagement quality control requirements should be directly linked to those established in ISQC 1. As a result, we would expect a change to restructure ISQC 1 would have a direct flow-through effect on engagement quality standards. We encourage the Board to address any revisions to ISA 220 simultaneously with ISQC 1 in order to ensure their continued integration. We also note there is no discussion of other assurance engagements in this document for comment. Engagements other than audits of historical financial information, conducted in accordance with other international assurance standards would be equally impacted by changes to ISQC 1. We would therefore encourage the engagement quality elements of these standards also be revised simultaneously with ISQC 1 to ensure

proper integration.

(d) If ISQC 1 is not restructured to require the firm's use of a QMA, do you believe that we should otherwise address the matters described in paragraph 59 and table 2, and if so, how?

If ISQC 1 is not restructured to require the use of a QMA, we would prioritize monitoring and the application of ISQC 1 for non-audit engagements (e.g., specified procedures, review engagements). We do not believe these are dependent on a QMA approach and that the important improvements noted in table 2 in respect of the above could be achieved within the existing structure of ISQC1. We also would recommend the Board ensure ISQC 1 requirements are consistent and properly integrated with engagement level quality requirements.

2. Engagement partner roles and responsibilities

(a) Paragraphs 69–86 set out matters relating to the roles and responsibilities of the engagement partner.

(i) Which of the actions outlined in paragraphs 85–86 would be most meaningful to address issues related to engagement partner responsibilities?

From a public sector perspective, the most meaningful issue to explore would be the matter of the expected performance requirements for individuals other than the engagement partners who sign or are named in the auditor's report as this issue is prevalent in the public sector, and further guidance concerning the role of the engagement leader throughout the engagement.

(ii) Why do you believe these actions are necessary?

We do not believe the majority of the actions outlined in paragraphs 85-86 are needed to enhance audit quality issues specific to the public sector beyond those already supported by existing firm and engagement level standards for audit quality.

For example, we believe the discretion currently afforded the engagement partner in respect of audit documentation review is appropriate. We also believe current audit quality requirements in respect of ensuring the capacity and competence of the audit team are adequate and that actions in respect of professional skepticism will have a greater impact on audit quality.

(iii) Are there other relevant issues that we should consider, or actions that would be more effective than those described? If you would not support a particular action, please explain why.

No unique public sector considerations were noted.

(iv) Describe any potential consequences of possible actions that you believe we need to consider further.

In respect of the matter outlined in paragraph 86 (expected performance requirements for individuals other than the engagement partners who sign or are named in the auditor's report), we hold the view that in addressing this issue, there is a risk of confusing stakeholders and detracting from of the fundamental roles and responsibilities of the engagement partner. Actions taken in this area should be directed at reinforcing the roles and responsibilities of the engagement partner and their application.

(b) Do you think it is necessary for the ISAs to include requirements or otherwise address the circumstances described in paragraph 79 in which an individual other than the engagement partner is required to or otherwise customarily sign(s) the auditor's report or is named therein? If yes, please explain why, and provide your views about how this could be done (including describing the work effort you believe would be necessary for such an individual).

As noted above, we support the value of such guidance and feel it is very relevant to the public sector.

In the public sector, an Auditor General may sign auditor's reports for engagement performed on his or her behalf by individuals assigned to the role of engagement partner. An Auditor General may have specific authority or obligations in respect of reporting established in law, regulation or custom. Engagement partners may be delegated authority to sign an auditor's report acknowledging the delegation in the published report.

Our views as to how to address the circumstances described in paragraph 79 are outlined in our response to question 2 (a)(iv). We believe there is no specific work effort incremental to that of the engagement partner that should be consistently applied other than that already established by a firm's system quality control. A properly designed and implemented system should result in a firm environment that appropriately promotes and maintains the necessary inputs to quality engagements. We would guide such individuals to apply their knowledge of the results of monitoring the system of quality control and external inspections, the maturity of the audit firm practice, the maturity of the accounting environment of the preparer (for example, the maturity and quality of applicable accounting frameworks and preparers' understanding of these frameworks), and the risks of particular engagements in order to properly assign/delegate engagement partners and Engagement Quality reviewers (where needed) to individual engagements. This same information should also be used to ensure the continued relevance and effectiveness of the firm's system of quality control.

3. Others involved in the audit

(a) Paragraphs 87–104 set out matters relating to involvement of others in the audit:

(i) Which of the actions outlined in paragraphs 100–104 would be most meaningful to address issues related to others participating in the audit?

From a public sector perspective, we would consider most meaningful the actions outlined in paragraph 100 to consider whether specific requirements and application material for two scenarios: first, where other auditors (that are not component auditors or not otherwise part of the engagement team) are involved in the engagement, and second, the actions outlined in paragraph 101 concerning the ability to use another auditor's report as audit evidence in certain circumstances.

(ii) Why do you believe these actions are necessary?

These actions are believed to be meaningful as both scenarios described in 3(a)(i) arise in practice and would benefit from either additional, practical guidance or confirmation of previous conclusions.

(iii) Are there other relevant issues that we should consider, or actions that would be more effective than those described? If you would not support a particular action, please explain why.

No unique public sector considerations were noted.

(iv) Describe any potential consequences of possible actions that you believe we need to consider further.

No potential consequences of possible actions have been identified.

(b) Should we develop further requirements or application material for circumstances when other auditors are involved in an audit engagement (i.e., auditors that don't meet the definition of component auditors)?

We support the development of additional requirements or application material in respect of circumstances when other auditors are involved in an audit engagement that are not component auditors as it should serve to improve and clarify the application of the audit quality standard to various team composition and emerging audit delivery models.

6. Engagement Quality Control Review (EQCR) and reviewers

(a) Paragraphs 136–146 set out matters relating to engagement quality control reviews and engagement quality control reviewers.

(i) Which of the possible actions outlined in paragraphs 143–146 would be most meaningful in addressing issues related to EQC reviews and EQC reviewers?

We support all of the actions outlined in paragraphs 143-146. From a public sector perspective, the actions that would be most meaningful are those directed at supporting a firm's identification of engagements other than audits of listed entities where an EQCR would be most valuable.

(ii) Why do you believe these actions are necessary?

In the public sector, audits of listed entities are rare. As a result, there is a significant risk that many public sector engagements will not be selected for engagement quality control review. Further, other assurance engagements (such as direct engagements) could be more explicitly addressed in current requirements.

(iii) Are there other relevant issues that we should consider, or actions that would be more effective than those described? If you would not support a particular action, please explain why.

The Invitation to Comment discussion of monitoring and remediation appropriately identifies that there are a variety of both pre-issuance and post-issuance reviews performed by firms attempting to address audit quality concerns or risks. We would support the Board considering how pre-issuance reviews or other pre-issuance activities could be integrated more explicitly into the system of quality control engagement performance elements in addition to the Board's current consideration that they may be an input to monitoring.

We do not support the proposed action of communicating in the auditor's report whether the engagement was subject to an EQC review. An EQC review is only one of the multitude of actions and procedures applied to address risks to audit quality. As such, it would appear inappropriate to draw specific attention to this specific element of the firm's system of quality control in the auditor's report.

(iv) Please also describe any potential consequences of possible actions that you believe we need to consider further.

It is important the Board recognize the integration of certain classification decisions and the consequences on the applicability of other requirements. For example, if changes are made to the concept or definition of listed entity, impacts on other standards such as auditor reporting must also be considered.

(b) Specifically:

(i) Should ISQC 1 mandate the performance of EQC reviews beyond audits of listed entities? If yes, what other entities should be considered and how could we best define these entities? If no, please explain your reasoning.

We agree that ISQC 1 could mandate the performance of EQR beyond audits of listed entities provided appropriate criteria and definitions are established that can be consistently applied in various jurisdictions. We do not believe the IAASB should only define the entity, but rather that the criteria should outline the nature of the engagement that would be most appropriately supported by the appointment of an engagement quality control reviewer as an additional requirement to audit quality risks. This criteria could include, as one element, the form of entity being audited (e.g. a pension plan).

(ii) Do you believe it is necessary for ISQC 1 to require that firms define the minimum period of time between when an individual has been the engagement partner and when that individual would be eligible to serve as the EQC reviewer on the same engagement? If yes, how do you think

this should be done and why? If no, please explain why.

We agree a cooling off period between the period of time an individual has been the engagement partner and when that individual would be eligible to serve as the EQC reviewer on the same engagement is appropriate. This issue could be addressed as a component of the IESBA code of ethics discussion of long association and rotation.

(iii) Would you support the development of a separate EQC review standard? Please explain the reasoning for your response.

We would support the development of a separate EQC review standard. This would serve to provide firms with more detailed requirements and guidance to support their implementation of the role. A separate standard would elevate the importance of the role and provide the opportunity to expand on how other activities of a firm, such as pre-issuance reviews, should be properly integrated into the system of quality control.

7. Monitoring and remediation

(a) Paragraphs 147–159 set out matters relating to monitoring and remediation.

(i) Which of the possible actions outlined in paragraphs 156–159 would be most meaningful in addressing issues related to monitoring and remediation?

From a public sector perspective, the actions that would be most meaningful are those directed at how the performance of pre-issuance and post-issuance reviews, and the results thereof, may factor into the firm's system of quality control, the role and results of external reviews and how these interact with the internal monitoring system, and the implementation of requirements to obtain an understanding of causal factors of identified audit deficiencies.

(ii) Why do you believe these actions are necessary?

The above actions would be an opportunity to improve the overall efficiency of monitoring the system of quality control given the extent of post-issuance reviews currently being performed. Public sector auditors also often elect to participate in independent peer reviews whose results are currently not a recognized component of monitoring. Further, public sector auditors may operate in an environment of organizational risk management and control in addition to that set out in ISQC 1. Both the AQM approach and a review of monitoring and remediation are an opportunity to further integrate these overlapping requirements to improve efficiency and effectiveness.

(iii) Are there other relevant issues that we should consider, or actions that would be more effective than those described? If you would not support a particular action, please explain why.

No unique public sector considerations were noted.

(iv) Please also describe any potential consequences of possible actions that you believe we need to consider further.

No potential consequences were noted for consideration.

(b) Specifically:

(i) Do you support the incorporation of a new requirement(s) in ISQC 1 for firms to understand the causal factors of audit deficiencies relating to inspection findings and other reviews? If not, why? Are there any potential consequences or other challenges of taking this action that you believe we need to consider?

We support the consideration of causal factors as best practice and new requirements for firms to understand the causal factors of audit deficiencies relating to inspection findings and other reviews.

(ii) Do you support the incorporation of a new requirement(s) in ISQC 1 for the results of the firm's monitoring of the effectiveness and appropriateness of the remedial actions to be considered in the design and assessment of the effectiveness of the firm's system of quality control? Please provide further detail to explain your response.

We support this incorporation as an appropriate monitoring consideration as this would align system monitoring with the design expectation.

10. Transparency reporting

(a) Do you believe we are able to positively contribute to the evolving developments related to transparency reporting? If so, what, in your view, would be the most appropriate action we could take at this time?

At this time, we would encourage the Board to continue to monitor industry developments in respect of transparency reporting. We do not see a role for the Board at this time.

(b) If you would not support us taking actions as described in paragraph 190(b), please explain why, including any potential consequences of those actions that you believe we need to consider.

We support the actions described in paragraph 190(b).

14. Are there any specific public sector considerations related to the issues and potential actions described in this section? Are there any other public sector considerations of which we should be aware? If so, please provide details and views about these matters.

We have identified public sector considerations related to the issues and potential actions in respect of audit quality in the above responses.

Group Audits

1. We plan to revise ISA 600 (and other standards as appropriate) to respond to issues with group audits. Should we increase the emphasis in ISA 600 on the need to apply all relevant ISAs in an audit of group financial statements? Will doing so help to achieve the flexibility that is needed to allow for ISA 600 to be more broadly applied and in a wide range of circumstances (see paragraphs 194–198)? If not, please explain why. What else could we do to address the issues set out in this consultation?

We support the IAASB's interest to increase the emphasis in ISA 600 on the need to apply all relevant ISAs. We believe improving the emphasis in the requirements and application guidance of ISA 600, particularly for relevant ISAs such as ISA 220, ISA 315, ISA 320, and ISA 330, would improve the guidance for group audit. In addition, we believe guidance and examples in the application guidance should be considered to address identified challenges, such as addressing matters related to an entity's use of a shared service center.

2. Which of the possible actions outlined in paragraphs 215–217 would be most meaningful in addressing issues related to acceptance and continuance procedures?

A legislative auditor may not have the option to decline or discontinue an audit. It is important and meaningful to acknowledge this public sector consideration. We support proposals to guide a group auditor by clarifying appropriate actions in situations involving the expected adequacy of sufficient and appropriate audit evidence.

We believe ISA 600 should include guidance for applying relevant ISAs in the consideration of acceptance or continuance of the group audit and that changes should be focused on providing additional

guidance to the group auditor rather than increasing requirements.

3. Which of the possible actions outlined in paragraph 224 would be most meaningful in addressing issues relating to communication between the group engagement team and the component auditor?

We believe that adding application guidance related to competency of the group engagement team, particularly having staff and an engagement partner at the group auditor able to handle component auditors using different languages, standards or regulatory frameworks, would address some of the issues related to group and component auditor communication. Instead of creating an additional standard for the component auditor, we suggest the following to improve the quality and timeliness of communication and documentation access to meet the needs of the group auditor.

- *Create additional application guidance to improve timely and effective two-way communication between the group and component auditor,*
- *Provide additional guidance and examples in the required and additional matters included in the group engagement team's letter of instruction, specifically related to the timeliness of the communications and access to documentation,*
- *In the Communication with the Component Auditor section of the application guidance, the component auditor cooperating with the group auditor guidance, outlined in paragraph A59, could be expanded to include examples of the types of documentation and the timeliness of the access to the documentation.*

4. Which of the possible actions outlined in paragraph 234 and 242 would be most meaningful in addressing issues related to using the work of the component auditor?

We believe the most meaningful action proposed would be to include in ISA 600 an explicit determination about whether it is appropriate for the group engagement team to use the work of a component auditor.

We also recommend that ISA 600 use examples in the application guidance to inform how a group engagement team might obtain an understanding of the component auditor.

5. Which of the possible actions outlined in paragraphs 251–253 would be most meaningful to address issues relating to identifying significant risks for the group audit?

We support providing examples in ISA 600 related to group audit materiality and the risk of material misstatement. If ISA 315 and ISA 330 are revised, we also support providing examples in these standards related to group audit materiality and the risk of material misstatement.

We also believe clarifying or adding application guidance related to a group auditor considering the significant risks identified by the component auditor would be meaningful in addressing the issues outlined.

6. Do you agree with the possible actions recommended in paragraph 261 to clarify the different aspects of materiality in a group audit? If not, please indicate which actions are not appropriate and describe why.

We believe that adding application guidance in ISA 600 reflecting different levels of materiality applicable to the component would help clarify issues related to materiality. The guidance should also link to ISA 320. We believe that if ISA 320 is considered for revision additional guidance and examples to reflect the materiality considerations at both the group and component auditor level should be included.

7. Which of the actions outlined in paragraphs 272–273, 279, 288 and 292 would be most meaningful to address issues relating to responding to identified risks of material misstatement in

a group audit?

Given the significant volume of consolidated entities and operations in consolidated financial statements of governments, the most meaningful action discussed in the above mentioned paragraphs from our perspective would be providing further guidance on how the group engagement team should determine which non-significant components require procedures and how to determine when a sufficient number of components have been selected for the performance of such procedures, notwithstanding that paragraph A53 of ISA 600 addresses, albeit to a limited degree, the situation where a group may be comprised of components that are non-significant components.

Similarly, while less significant, we also support revisiting the interaction between the definition of a component and the description of the consolidation process in ISA 600 to add clarity to the application of ISA 600.

8. Which of the actions outlined in paragraphs 299 and 303 would be most meaningful in addressing issues relating to the review and evaluation of the work of component auditors by the group engagement team?

Of the actions outlined in the above noted paragraphs, we believe the most meaningful action to be strengthening the requirement in paragraph 42(b) of ISA 600, and the related application material, to clarify the necessary work effort of the group engagement team in relation to reviewing the component auditor's working papers.

9. How should the matters set out in paragraphs 304–305 be addressed in our plans to revise ISA 600? Are there any other implications from our new or revised standards that should be considered?

We support the development of additional requirements and application guidance for communicating key audit matters to the group engagement team for consideration in forming the auditor's report on the group financial statements.

10. Are there any other issues relating to group audits that we have not identified? If yes, please provide details. What actions should we take to address these issues?

11. Are there any other specific actions that others could take in relation to group audits? If yes, please provide details.

12. Are there any specific considerations for SMPs related to the issues and potential actions described in this section? Are there any other considerations for SMPs of which we should be aware? If so, please provide details and views about these matters.

13. Are there any specific public sector considerations related to the issues and potential actions described in this section? Are there any other public sector considerations of which we should be aware? If so, please provide details and views about these matters.

We have not identified any other issues relating to group audits including specific public sector considerations other than those already identified in the invitation to comment and in our responses to the preceding questions concerning group audits.