

**Minutes of the 81<sup>st</sup> Meeting of the  
INTERNATIONAL AUDITING AND ASSURANCE STANDARDS BOARD  
Held on December 5–9, 2016 in New York, NY**

**Voting Members**

Present: Arnold Schilder (Chairman)  
Charles Landes (Deputy Chair)  
Abhijit Bandyopadhyay  
Jean Blascos  
Fiona Campbell  
Robert Dohrer  
Karin French  
Marek Grabowski  
Merran Kelsall  
Annette Köhler  
Brendan Murtagh  
Marc Pickeur  
Ron Salole (December 5 – 7 & 9)  
Rich Sharko  
Sayaka Sumida  
Imran Vanker  
Ge Zhang  
Megan Zietsman

**Technical Advisors**

Sara Ashton (Ms. French)  
Nicolette Bester (Mr. Vanker)  
Wolf Böhm (Prof. Köhler)  
Dora Burzenski (Ms. Zietsman)  
Chun Wee Chiew (Mr. Murtagh)  
Shu Duan (Mr. Zhang)  
Ahava Goldman (Mr. Dohrer)  
Hiram Hasty (Mr. Landes)  
Rene Herman (Ms. Kelsall)  
Josephine Jackson (Mr. Grabowski)  
Susan Jones (Mr. Blascos)  
Sachiko Kai (Ms. Sumida)  
Jamie Shannon (Mr. Sharko)  
Eric Turner (Mr. Salole)  
Inge Vanbeveren (Mr. Pickeur)  
Sanjay Vasudeva (Mr. Bandyopadhyay)  
Denise Weber (Ms. Campbell)

Apologies: -

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**Non-Voting Observers**

Present: Matthew Waldron (IAASB Consultative Advisory Group (CAG) Chairman), Atsushi Iinuma (Japanese Financial Services Authority)

Apology: Juan Maria Arteagoitia (European Commission)

**Public Interest Oversight Board (PIOB) Observer**

Present: Prof. Karel Van Hulle

## IAASB Technical Staff

Present: Beverley Bahlmann, Brett James, Vijyata Kirpalani, Natalie Klonaridis, Csilla Molnar, Schuyler Simms, Jasper van den Hout, Bradley Williams, James Gunn (Managing Director, Professional Standards)

International Auditing and Assurance Standards Board (IAASB) agenda materials referred to in these minutes can be accessed at <http://www.iaasb.org/meetings/new-york-usa-14>. These minutes are a summary of the decisions made at the December 2016 IAASB meeting, in light of the issues and recommendations in the agenda material put forth by the Task Forces, Working Groups, Drafting Teams and Staff supporting the individual projects. These recommendations are made taking into account feedback from respondents to the IAASB's public consultations, in particular Exposure Drafts (EDs) of the IAASB's proposals, consideration of previous discussions of the Board and its CAG, and feedback from stakeholders through outreach activities.

### 1. Welcome and Approval of Previous Minutes

The minutes of the September 19-23, 2016 IAASB meeting, with one amendment to what was presented, and the November 1, 2016 IAASB teleconference, as presented, were approved.

### 2. ISA 540<sup>1</sup>

Mr. Sharko and Mr. Pickeur introduced the topic by highlighting the objectives of the project to revise ISA 540 and timeline for moving the project forward. They also explained the reasons for seeking approval of the ED in March 2017 instead of December 2016.

#### INTRODUCTION

Mr. Sharko explained that the ISA 540 Task Force (ISA 540 TF) discussed the Introduction section but that further changes will be made to the application material to explain the key characteristics of accounting estimates, including the factors of complexity, judgment, and estimation uncertainty. The Board generally supported the ISA 540 TF's proposals but suggested consideration of the following:

- Explaining the interaction between ISA 315 (Revised)<sup>2</sup> and ISA 540 in the Explanatory Memorandum to the ED, including the interaction between the factors of complexity, judgment and estimation uncertainty and the four factors that are introduced by the ISA 315 (Revised) Task Force in **Agenda Item 10-A**;
- Limiting the additions to the application material, as it was noted that excessive amounts of guidance can make the introduction section less clear. It was suggested that some of the introduction and related application material could be included in an Appendix to the standard; and
- Adding back the notion of management bias in the Introduction section as it helped to explain the focus of the ISA.

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<sup>1</sup> ISA 540, *Auditing Accounting Estimates, Including Fair Value Accounting Estimates, and Related Disclosures*

<sup>2</sup> ISA 315 (Revised), *Identifying and Assessing the Risks of Material Misstatement through Understanding the Entity and Its Environment*

## DEFINITIONS AND RISK ASSESSMENT

The Board generally noted support for the definitions and the risk assessment section but asked the ISA 540 TF to consider:

- Including the notion of estimation uncertainty in the definition of an accounting estimate;
- Broadening the reference to data in paragraph 8(c)(iA) and paragraph 8(c)(ii) beyond just external data;
- Simplifying paragraph 8, as some Board members were of the view that the current construct could be seen as complicated and long; and
- Broadening the scope of paragraph 9A and 11A by noting that the auditor should think about whether specialized skills or knowledge are needed throughout the audit rather than just specific phases of the audit. It was suggested to look at the guidance provided by the United States Public Company Accounting Oversight Board (PCAOB).

It was noted that the application material to paragraph 9 could be enhanced by clarifying the objective of the retrospective review and explaining when performing a retrospective review would not be useful. The Board also suggested deleting paragraph 10(d) and including application material that explains that the auditor may also take other factors into account in the assessment of the risk of material misstatement.

## WORK EFFORT

The majority of the Board supported a threshold to direct the auditor when the more detailed work effort requirements are mandatory as it was seen to help practitioners navigate through the standard and improve the clarity and understandability of the standard. However, the Board asked that the threshold be made as clear and understandable as possible.

The Board generally supported a requirement in ISA 540 that expands on when substantive procedures alone cannot provide sufficient appropriate audit evidence (option 1 as presented in **Agenda Item 2-A**). This was because it was seen to be responsive to concerns expressed by certain regulators that, without such a requirement, ISA 540 could be seen as lacking rigor regarding the importance of testing the operating effectiveness of controls in certain circumstances.

In addition the Board generally asked the ISA 540 TF to consider:

- Simplifying paragraph 13 and thereby enhancing the readability and understandability of the standard. The Board noted that the current requirement are comprehensive but complex.
- With respect to stand back requirement in paragraph 13D:
  - Whether the requirement should be performed for accounting estimates generally or individually;
  - Emphasizing the importance of professional skepticism in the stand back requirement;
  - Broadening the requirement so that it is based on the audit procedures performed in accordance with ISA 540 instead of just the work effort requirements; and

- o Aligning the requirement more closely with ISA 330<sup>3</sup> and ISA 570 (Revised).<sup>4</sup>

The Board supported the objective-based approach in paragraphs 13A-C as presented by the ISA 540 TF and provided several suggestions for how to enhance these paragraphs. These suggestions included making certain of the paragraphs more objective based, and clarifying and simplifying other paragraphs.

#### OTHER MATTERS

The Board had mixed views on whether external information sources should be addressed by the ISA 540 TF or the Working Group that may be formed for a potential project related to Audit Evidence. The majority of the Board supported the ISA 540 TF's view that, as set out in **Agenda Item 2-D**, the ISA 540 TF should address external information sources. In making this decision, the Board noted that any changes to ISA 500<sup>5</sup> should be limited to external information sources and that the ISA 540 TF should be mindful of the risk of unintended consequences to aspects of the audit not related to accounting estimates. It was also agreed that this matter should be highlighted in the Explanatory Memorandum to be issued with the ED. The Board requested that consideration be given to broadening the application material related to external information sources by including examples that are not pricing-related as the application material presented is heavily focused on pricing services.

The Board also requested consideration of the following other matters in the agenda material:

- Including application material that provides guidance for when the auditor's range is large (such as when the auditor's range larger than performance materiality);
- Evaluating whether all the application material is needed. It was noted that some of the application material could be used in an International Auditing Practice Note (IAPN) on banking specific matters;
- Addressing the remaining matters suggested by the Professional Skepticism Working Group to enhance professional skepticism in auditing accounting estimates;
- Whether the documentation requirement could be broadened to include additional matters;
- Making changes to the requirements to improve the clarity, understandability, and conciseness as some requirements are complex and therefore may lead to confusion and implementation issues; and
- Considering whether all matters included in the project proposal and project update have been addressed.

#### IAASB CAG CHAIRMAN'S REMARKS

Mr. Waldron noted that the standard as presented takes into account suggestions made by CAG Representatives. He furthermore highlighted the importance of having a standard that is understandable and noted that the CAG was generally supportive of approving an ED in March 2017, noting that it is better to approve the ED later in order to get a high-quality standard.

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<sup>3</sup> ISA 330, *The Auditor's Responses to Assessed Risks*

<sup>4</sup> ISA 570 (Revised), *Going Concern*

<sup>5</sup> ISA 500, *Audit Evidence*

#### PIOB OBSERVER REMARKS

Prof. Van Hulle reminded the Board that it was important to address the key messages it receives from stakeholders, including the Basel Committee on Banking Supervision and the International Association of Insurance Supervisors. To that end, he suggested including more requirements specifically related to models to respond to their comments.

With respect to the work effort, Prof. Van Hulle noted that this section can be perceived as being extremely complex and suggested simplifying the standard by reinforcing a principles-based approach and trying to simplify the language.

#### WAY FORWARD

The IAASB will discuss ISA 540 again at its teleconference in January, 2017 and its meeting in March 2017. The Task Force intends to present a draft ED for approval at the March 2017 IAASB meeting.

### **3. Innovation**

Mr. Landes introduced the topic and provided an update on the activities of the Innovation Working Group (IWG), which included consideration of the feedback from various stakeholders on the IAASB's recent 2017–2018 Work Plan Consultation and innovation topics that are currently being explored by national standard setters globally. Mr. Landes provided an update on the American Institute of Certified Public Accountants' project on cybersecurity and Mr. Böhm provided an update of the Institut der Wirtschaftsprüfer's work on assurance of governance, risk, internal control, internal audit and compliance.

#### NON-GAAP FINANCIAL MEASURES

The Board discussed the auditor's role with respect to non-GAAP financial measures (also referred to as alternative performance measures). The Board provided the following insights on the role of the IAASB's International Standards in relation to non-GAAP financial measures:

- Regulators may need to first address these measures in terms of establishing more robust criteria for entities to comply with.
- In some jurisdictions, there is assurance provided on these measures that is performed under the existing IAASB standards.
- Assurance could focus on the process for determining the measure (i.e., that it ties back to the financial statements), rather than the measure itself.
- In developing ISA 720 (Revised),<sup>6</sup> the Board considered the use of alternative performance measures and accordingly the evaluation of a need for a standard-setting response could be considered as part of the planned auditor reporting post-implementation review.

The Board concluded that, at this stage, there is not a need for a specific response from a standard-setting perspective as there is currently not a demand for separate assurance on these measures.

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<sup>6</sup> ISA 720 (Revised), *The Auditor's Responsibilities Relating to Other Information*

## BLOCKCHAIN TECHNOLOGY

The Board discussed the possible impact of blockchain technology on the auditing profession, and noted concerns regarding the security of this technology and the ability to change the underlying data or information. The Board also noted that globally regulators are contemplating necessary measures to control this technology in the interests of the public.

## IAASB CAG CHAIRMAN'S REMARKS

Mr. Waldron indicated that the topic of non-GAAP financial measures is an area of interest for investors, noting that investors perceive these measures as informative regarding the conduct of management, in particular the degree of their efforts in developing such measures. He noted that there may be a demand in the future for assurance of these measures. Mr. Waldron also highlighted some of the research published in relation to blockchain technology.

## WAY FORWARD

The IWG will continue its monitoring activities. It was suggested that the topic of blockchain technology should be discussed with the NSS Liaison Group at its June 2017 meeting, as well as with the Board in June or September 2017 through inviting a panel of specialists from different industries to help the Board understand the accounting and auditing implications.

## **4. The IAASB's Work Plan for 2017–2018 and Continuing Relevance of Its Strategic Objectives**

Prof. Schilder introduced the topic, noting that the overall message from respondents to the IAASB's [Survey Consultation—The IAASB's Work Plan for 2017–2018 and Continuing Relevance of Its Strategic Objectives](#) (the Survey Consultation) was for the IAASB to continue focusing on its existing priority projects before commencing new projects. He further explained the rationale behind the projects included in the draft Work Plan for 2017–2018 (the Work Plan).

In its letter to the IAASB, the International Federation of Accountants (IFAC) Small and Medium Sized Practices (SMP) Committee expressed support for the draft Work Plan, particularly the continuing focus on understanding the issues and implementation needs of SMPs and the inclusion of a project related to Agreed-upon Procedures (AUPs). The SMP Committee also noted the need for clearer guidance in the standards related to documentation, which remains a challenge in smaller audits.

Ms. Bahlmann highlighted that the International Organization of Securities Commissions (IOSCO) had noted that the IAASB should prioritize the projects communicated in 2014 – audit evidence, professional skepticism, and work of other auditors and experts. IOSCO urged the IAASB to commit resources to these important efforts rather than other initiatives such as integrated reporting and other emerging developments in external reporting, agreed-upon procedures, and consideration of matters related to SMPs and audits of small- and medium-sized entities (SMEs).

In relation to the Work Plan (including the proposed forward timetable for completion of the projects), IAASB members commented as follows:

- That the Work Plan is ambitious, particularly given the fundamental nature of the issues being addressed and the interrelationship between the standards (including the need to sequence some of the revisions), highlighting that there is little contingency for other efforts that may be needed during the period. Prof. Schilder responded that notwithstanding that there appeared to be a significant commitment to the planned projects, there would still be flexibility should the need arise, for example

by slowing down projects or delaying the commencement of new projects. IAASB members therefore highlighted the importance of being transparent about changes to the targeted timetable.

- That it is not clear what the project on AUP involves.
- That there is insufficient detail about the coordination efforts with the International Ethics Standards Board for Accountants (IESBA), in particular how IAASB efforts will be identified if something arises in the IESBA's work program that needs to be addressed in the IAASB's standards.
- That it was not clear for the way forward on the topics that were not topics scheduled to commence in the 2017–2018 period, but that had been highlighted as important by respondents to the survey, for example going concern. Prof. Schilder noted that going concern would be considered as part of the auditor reporting post-implementation review, and the outcome of that review would help the IAASB determine future efforts in this area.
- That although sufficient input was obtained from most stakeholder groups (e.g., regulators and audit oversight bodies) on the IAASB's future efforts, it was questioned how input from users was obtained. Prof. Schilder noted that this was a continuing struggle, but that more effort was being made for dialogue with investor groups, and that these efforts would continue to be focused on in 2017.
- In relation to the timetable, IAASB members commented variously about consistency and the planned timing for various activities, for example the development of International Auditing Practice Notes. In addition, it was questioned what time would be available to analyze the responses to the Integrated Reporting Working Group Discussion Paper, [Supporting Credibility and Trust in Emerging Forms of External Reporting: Ten Key Challenges for Assurance Engagements](#) (EER Discussion Paper) and for the way forward on this initiative.

Changes made to the Work Plan (and forward timetable) to address Board comments included:

- Highlighting the ambitious nature of the Work Plan, and clarifying that the IAASB's priorities may change in light of national and international developments and that the progression of the projects may follow different timelines to completion given the nature of the issues being addressed.
- Highlighting that the IAASB will be transparent about changes to the targeted timetable.
- Clarifying that the IAASB will focus its efforts on its current key topics, and new projects will be undertaken if and when it is realistically feasible.
- Highlighting the IAASB's focus on scalability and proportionality in the projects to be undertaken.
- Clarifying that the AUP project, subject to support from stakeholders in response to a Discussion Paper, [Exploring the Demand for Agreed-Upon Procedures Engagements and Other Services, and the Implications for the IAASB's International Standards](#), will focus on the revision of ISRS 4400,<sup>7</sup> with further consideration of the IAASB's actions in relation to the other aspects of the Discussion Paper, including as it relates to multi-scope engagements, to be determined once the responses have been analyzed.
- Providing further details about the coordination efforts with IESBA on matters that may impact either the Code of Ethics for Professional Accountants (the IESBA Code) or the IAASB's International Standards, with coordination efforts to continue at Staff, Board and respective leadership levels.

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<sup>7</sup> International Standard on Related Services (ISRS) 4400, *Engagements to Perform Agreed-Upon Procedures Regarding Financial Information*

- Clarifying that the post-implementation review of the IAASB's new and revised Auditor Reporting standards will include evaluation of experience with key audit matters and with communications in the auditor's report relating to going concern and materiality, as well as experience with the implementation of revised ISA 720.<sup>8</sup>
- Including time for the considerations of responses to the EER Discussion Paper with clarification that responses were to be analyzed during 2017, and an appropriate way forward on this topic determined at that time.

#### IAASB CAG CHAIRMAN'S REMARKS

Mr. Waldron noted that a teleconference was held with CAG Representatives to discuss the responses to the Survey Consultation and the Work Plan. He highlighted that CAG Representatives broadly supported the Work Plan and related priorities, noting that on balance the proposals reflected the responses received to the Survey Consultation. He explained that mixed views were expressed by CAG Representatives relating to the proposed project on AUPs, with some CAG Representatives highlighting the importance of the stakeholders that would benefit from such a project (e.g., SMPs), while others noted the view that the IAASB should consider audit related projects to be of higher priority than projects on topics not audit-related, particularly if the allocation of the Board's resources toward a project on a non-audit related topic resulted in delays in the Board's priority ISA projects.

In relation to the forward timetable, which was recognized by CAG Representatives as ambitious, Prof. Schilder noted that CAG Representatives emphasized the need to develop quality standards and revisions over speed of completing the projects too quickly.

Mr. Waldron highlighted that the IAASB was urged to provide transparency about the progression of the projects in 2017–2018, in particular when there is a delay or change in the targeted timeline, or a new topic arises that the IAASB needs to address, with communication about how these changes affect the timeline of the Board's existing projects.

#### APPROVAL

The IAASB unanimously approved its Work Plan for 2017–2018, with 18 affirmative votes out of the 18 IAASB members present, signaling a commitment to enhancing audit quality by prioritizing and completing the significant projects commenced in the 2015–2016 period. The IAASB also confirmed the continuing relevance of its strategic objectives through a mid-period review, and will publish a Supplement to its Strategy for 2015–2019 to communicate this to its stakeholders.

#### WAY FORWARD

The IAASB's Work Plan for 2017–2018 and the Supplement to the IAASB's Strategy for 2015–2019 on the Continuing Relevance of the Strategic Objectives will be published once the PIOB has approved due process.

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<sup>8</sup> ISA 720 (Revised), *The Auditor's Responsibilities Relating to Other Information*

## 5. Quality Control – ISQC 1

Ms. French provided an overview of the Quality Control Working Group's (QCWG) recommendations on the possible approach to revising ISQC 1<sup>9</sup> to incorporate quality management, as presented in **Agenda Item 6-A**. Ms. French provided feedback from the Small and Medium sized Practices (SMP) Committee, highlighting its support for the proposals and the components and their agreement that the proposals would keep the standards robust. She noted, however, their concerns that the proposals could be an add-on to the existing requirements of ISQC 1 and the SMP Committee's encouragement to ensure the standards are scalable. She added that the SMP Committee encouraged the IAASB to keep the standards clear and simple, to think about the appropriate placement of the examples and to consider how the incorporation of quality management would operate in networks of firms.

The Board was supportive of the overall direction proposed by the QCWG, but emphasized the importance of the change management related to this project, including considering what the proposals are expected to achieve, how the proposals would change behaviors and the impact on audit firms, as well as how regulators inspect audit firms. The Board encouraged the QCWG to improve the linkage of ISQC 1 to the Audit Quality Framework,<sup>10</sup> and to consider the applicability of the proposals to other services as the standard is developed.

### COMPONENTS OF QUALITY MANAGEMENT

The Board was supportive of the proposed components of quality management and how these were depicted in the diagram to reflect how they inter-relate. The Board provided the following suggestions:

- Governance and leadership are important to the effective functioning of the firm's quality management, however "governance and leadership" are elements that exist outside of the firm's quality management and should be articulated in terms of the role they play in the firm's quality management.
- "Organization, culture and strategy that foster quality" should be presented as a separate component from "governance and leadership", as this is a fundamental element of quality management that could be understated if it were subsumed as part of "governance and leadership". Furthermore, the link between "governance and leadership" and "organization, culture and strategy that foster quality" needs to be clear, as well as any relationship between firm culture and ethical considerations.
- Given the fundamental nature of "monitoring and remediation", it may warrant more prominence than how it is depicted or implied in **Agenda Item 6-A**.
- "Information, communication and documentation" are not foundational components for effective quality management, but are rather important measures needed to support effective quality management. Furthermore, documentation is conceptually a subset of information and communication and accordingly should not be incorporated in the heading.
- The difference between "quality management" and the "quality management process" needs to be clarified, as well as what is considered to be components of quality management and elements of applying the quality management process. Clarification of other terminology was also recommended

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<sup>9</sup> ISQC 1, *Quality Control for Firms that Perform Audits and Reviews of Financial Statements, and Other Assurance Engagements and Related Services Engagements*

<sup>10</sup> *A Framework for Audit Quality: Key Elements that Create an Environment for Audit Quality*

and there were some suggestions to align the terminology with that used in the COSO Integrated Framework.<sup>11</sup>

#### ROBUSTNESS OF ISQC 1

The Board was of the view that more specific details of how the proposals would be developed is necessary to support the understanding of whether the robustness of ISQC 1 would be retained. The Board also recommended that the requirements be established in terms of levels, through establishing outcomes-based or principles-based requirements at an overall level, providing flexibility in terms of their implementation, with a further layer of more specific requirements.

#### SCALABILITY OF ISQC 1

The Board agreed with the QCWG's suggestions on how to incorporate scalability in ISQC 1, and provided the following additional comments and questions:

- What is meant by “scalability” and “proportionality” needs to be clarified in order to facilitate the development of the requirements.
- How the concepts of quality management would apply in the circumstance of networks of firms is important to being able to demonstrate scalability.
- Being clear about at what level the “quality management process” would be applied within the firm, including whether it applies to all services, would be necessary to establishing the scalability of ISQC 1.
- The use of terminology is important, for example, “informal” has connotations that the firm does not need to have very rigorous quality management and would be better contextualized as “simple.”

#### QUALITY MANAGEMENT PROCESS

The Board noted that this would be an area that would be particularly challenging for SMPs to implement. The Board also had various suggestions relating to the proposals in respect of the requirements for the quality management process:

- With respect to the assessment of the risks to quality, the Board cautioned that this should not be confused with performing the assessment of risks of material misstatement as contemplated in ISA 315 (Revised), and the assessment should be based on an understanding of the engagements performed by the firm.
- Consistent with the COSO Integrated Framework, the firm would need to establish its risk tolerance, linked to obtaining a reasonable level of assurance regarding the effectiveness of its quality management.
- There should be recognition in ISQC 1 that responses to quality risks may be established by the firm but are implemented at an engagement level.
- It was suggested that “re-evaluating the QMP” should not be a discrete element, and that this would be part of monitoring and remediation and the assessment by firm leadership of the effectiveness of the firm’s quality management.

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<sup>11</sup> Committee of Sponsoring Organizations of the Treadway Commission *Internal Control – Integrated Framework*

#### APPLYING THE QUALITY MANAGEMENT PROCESS

The Board did not agree with the use of the phrase “at a minimum” to indicate that the objectives and responses are the minimum required in addition to the firm’s own evaluation of its quality objectives and responses, as it was perceived that this could create unintended consequences. The Board encouraged the QCWG to establish well-defined objectives that clarify what is considered to be quality. The Board recommended that the identification and assessment of risks to quality also needs to be included in order to support the requirement being scalable and proportional and that the term “responses” be considered in the context of other control frameworks and the terminology in the ISAs. The Board cautioned that the existing requirements of ISQC 1 would need to be carefully considered as they are updated and transposed.

#### PIOB OBSERVER REMARKS

Prof. Van Hulle highlighted the importance to the public interest of establishing requirements that support consistent audit quality across firms globally.

#### WAY FORWARD

The QCWG will consider the Board’s comments in further developing the revisions to ISQC 1, as well as considering what outreach will be necessary in 2017 in order to establish how the proposals may impact firms and regulators. The QCWG will present their further recommendations to the Board at its March 2017 meeting, in particular in relation to monitoring and remediation, governance and leadership and information, communication and documentation.

### 6. Engagement Quality Control (EQC) Review

Ms. French introduced the topic of engagement quality control (EQC) reviews and provided an overview of the SMP Committee feedback in respect of the issues presented in **Agenda Item 7-A**. She explained that the SMP Committee was supportive of the proposed changes to the timing of the EQC review, however provided various suggestions and comments on the proposed objective and definition, mostly relating to the clarity and appropriateness of certain aspects of the objective and definition. Ms. French explained that the SMP Committee was concerned with the proposed scope of engagements subject to an EQC review and were of the view that the proposals are going beyond what is needed to address the public interest. She also noted the SMP Committee’s views on the execution of the EQC review, in particular that the public interest is a necessary driver of the required review procedures and that the determination of whether further review procedures should be performed should not rest solely with the EQC reviewer. Ms. French also noted the SMP Committee’s recommendation to bring more emphasis to the roles and responsibilities of the EQC reviewer.

The Board in general agreed with the direction of the Quality Control Other Working Group’s (QCOWG) proposals for EQC reviews and provided the following recommendations:

- In relation to the objective and the definition of the EQC review, reinstate the concept that the EQC review should be completed on or before the date of the report while retaining the proposal that the EQC review should be performed at appropriate stages during the engagement and modify the language to encapsulate all circumstances when an EQC review is performed.
- In relation to the scope of the engagements that are subject to an EQC review:

- Focus on the risks being addressed by the EQC review in developing the requirements, and that they appropriately capture engagements that have significant judgments, while ensuring that how the requirements are articulated will be understandable in practice.
- Consider the appropriateness of certain factors proposed, and other factors that may also be relevant in determining when an EQC review should be performed.
- Bring more prominence to the fact that the EQC review is one of a number of controls that may be implemented by a firm in addressing quality risk.
- In relation to the execution of the EQC review:
  - Modify the requirements to address circumstances where there are no distinct “stages” in performing the engagement and reinstate the extant requirements related to the consideration of the financial statements, or other relevant subject matter.
  - Link the extent of the EQC review to the areas of quality risk that have been identified at the engagement level in accordance with ISA 220,<sup>12</sup> and also take into consideration issues raised by regulators and audit committees.
  - Exercise caution in including examples of significant judgments in the application material to avoid creating a “checklist mentality”.
  - Clarify the requirements relating to which documentation should be inspected by the EQC reviewer including that judgment may be applied in selecting that documentation.
  - Enhance the requirements addressing the documentation of the performance of the EQC review.

#### PIOB OBSERVER REMARKS

Prof. Van Hulle noted that an audit failure would not only impact the stakeholders of the audited entity, but could also impact the reputation of the firm and of the profession as a whole. Furthermore, he suggested that the category of entities for which EQC review is required be extended to include public interest entities. He explained that financial institutions are by definition in the public interest and, as such, should be subject to an EQC review. He expressed his support for the inclusion of a risk based assessment by firms to determine entities additional to those required by the standard, to be subject to an EQC review.

#### WAY FORWARD

The QCOWG will consider the Board's comments in further addressing the enhancements to EQC reviews. The QCOWG will present their recommendations on the eligibility of the EQC reviewer to the Board at its February 2017 teleconference.

### 7. Quality Control – ISA 220

Ms. Zietsman presented the Board with the Crossover Working Group's (Crossover WG's) initial views on possible revisions to ISA 220 from the responses to the ITC as set out in **Agenda Items 8-A and 8-B**. The possible revisions included suggested enhancements to many of the extant requirements and application guidance in ISA 220, the introduction of possible new requirements to embed quality management

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<sup>12</sup> ISA 220, *Quality Control for an Audit of Financial Statements*

principles at the engagement level and to address communications among members of the engagement team and others involved in the audit.

There was general agreement from the Board on the direction of the proposed enhancements put forward by the Crossover WG, with some areas for further consideration by the Task Force noted variously by Board members, including:

- Although supporting linking the objective of the auditor to managing quality of the audit, it was noted that more clarity about how this would be operationalized in ISA 220 is required (in particular the interaction between a risk assessment for these purposes (i.e. risks to quality) versus the assessment of the risks of material misstatement as required by ISA 315 (Revised));
- Support for clarifying the engagement partner's (EP) overall responsibility and accountability for audit quality at the engagement level, while still allowing the EP the flexibility to assign certain responsibilities to other members of the engagement team;
- Further consideration of situations where the signing partner is different from the EP who was responsible for the direction supervision, and review of the work performed as a part of the audit;
- The need for appropriate coordination with the IESBA relating to considerations around the definitions of EP, engagement team, and network firms;
- Support for a new requirement related to strengthening two-way communication among the members of the engagement team and those involved in the audit; and
- Support for further consideration of how firms in networks interact, especially as relates to quality control

#### PIOB OBSERVER REMARKS

Prof. Van Hulle encouraged the Task Force to further consider supervision of auditors where audit work has been outsourced (e.g., to other auditors), in particular as it relates to responsibilities for direction, supervision and review as well as communication.

#### WAY FORWARD

The Crossover WG will continue to progress possible changes to ISA 220 for discussion by the IAASB at future meetings, including further considering how to embed quality management principles at the engagement level.

### **8. Quality Control and Groups Audits Project Proposal**

Ms. Zietsman provided the Board with an overview of **Agenda Item 9-A, *Enhancing Audit Quality: Project Proposal for the Revision of the IAASB's International Standards Relation to Quality Control and Group Audits*** (the draft project proposal), addressing the revision of ISQC 1, ISA 220, and ISA 600.<sup>13</sup>

Ms. Zietsman noted the CAG Representative's support for the projects, in particular quality control and addressing the issues of governance in firms, engagement partner compensation and EQC reviews. Ms. Zietsman highlighted the CAG Representative's focus on scalability, audits of small- and medium sized entities and networks of firms. She also highlighted that CAG Representatives encouraged the IAASB to

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<sup>13</sup> ISA 600, *Special Considerations—Audits of Group Financial Statements (Including the Work of Component Auditors)*

consider how quality is effectively managed when making use of different experts throughout the network, and the potential impact on the projects of the long-term developments with respect to the IAASB's professional skepticism project. Ms. Zietsman also noted a CAG Representative's comment relating to how the changes will be executed, and whether the proposals for changes align with the original intent as set out in the project proposal.

Ms. Zietsman also highlighted that discussions with the International Forum of Independent Audit Regulators (IFIAR) Standards Coordination Working Group (SCWG) had taken place, explaining that the key discussion points were largely focused on the responses to the Invitation to Comment, *Enhancing Audit Quality in the Public Interest: A Focus on Professional Skepticism, Quality Control and Group Audits*. She highlighted that the IFIAR SCWG was supportive of the projects, emphasizing the importance of professional skepticism. Ms. Zietsman noted that the IFIAR SCWG had various questions on what a "quality management approach (QMA)" would look like in ISQC 1, the practical implications of implementing a QMA and how scalability would be achieved. She added that the IFIAR SCWG was supportive of moving forward on addressing EQC reviews, emphasized the importance of understanding the entity in managing quality and indicated their preference for accelerating the timing of group audits project.

Ms. Bahlmann indicated that as part of due process, the project proposal is distributed to the committees of the IFAC, as well as the other standard-setting boards (i.e., the IESBA, the International Accounting Education Standards Board (IAESB) and the International Public Sector Accounting Standards Board). Ms. Zietsman noted the key comments from this process, including:

- The need for close coordination with the IESBA and IAESB, including alerting them in timely manner regarding any new issues that could have implications for their respective standards.
- The learning outcomes established by the IAESB in their standards may need to be revised in light of the proposed changes to ISQC 1 addressing quality management and linking engagement partner competency to audit quality.

Ms. Bahlmann noted that the SMP Committee supported the proposed projects, with an emphasis that the IAASB should focus on the implementation issues that small-and medium-practices might encounter.

#### APPROVAL

After providing various editorial comments, the IAASB unanimously approved the project proposal to revise ISQC 1, ISA 220 and ISA 600 with 18 affirmative votes out of the 18 IAASB members present.

## 9. Professional Skepticism

Prof Köhler presented **Agenda Item 5-A** to the Board and provided an update of the activities of the Professional Skepticism Working Group (PSWG) since the September 2016 Board meeting. Prof Kohler highlighted the work streams being pursued by the different Boards, and explained that it is not clear what the IAESB is interested in with the planned literature review, but that she would report back to the Board with this information.

#### JOINT PSWG ACTIVITIES

Prof. Kohler highlighted that the PSWG will develop a joint Professional Skepticism stakeholder communication that would give prominence to the work, individually and in coordination, that the standard-setting boards (SSBs) will be undertaking in response to the feedback received by all three SSBs. The IAASB asked the PSWG to clarify:

- The purpose of the stakeholder communication and whether it would seek to obtain additional feedback in some way or serve as an “awareness” piece.
- What is meant by “call to action” and to whom it relates.

#### EXPLORING FUNDAMENTAL CHANGES TO THE CONCEPT OF PROFESSIONAL SKEPTICISM

The following views were expressed about the PSWG’s discussion of the potential changes to the concept of professional skepticism within the ISAs:

- Concern with the practicality of “No definition of professional skepticism” as an option being analyzed by the PSWG.
- A shift to presumptive doubt would be challenging, while one Board member commented that in his particular jurisdiction, an auditor is not permitted to accept an engagement if he or she has doubts about management.
- Related to the potential option of extending professional skepticism to all professional accountants (PAs), there was the view that the mindset of an auditor is different from that of a professional accountant and that the auditor’s questioning mindset has a clear object, management. But in the case of a professional accountant, who would be the object of their questioning/critical mindset?

The IAASB representatives of the PSWG will focus the analysis of implications and unintended consequences of the following options: 1) A requirement to seek out contradictory evidence, 2) a shift to a more challenging mindset or presumptive doubt, and 3) introducing a concept of levels of professional skepticism.

#### IESBA SHORT-TERM PROPOSED LANGUAGE

Mr. Richard Fleck (IESBA Deputy Chair and PSWG member) provided the Board with an update regarding the short-term proposals to be considered by the IESBA at its meeting the following week from December 12<sup>th</sup>–16<sup>th</sup>. The Board provided the following feedback to the IESBA representatives:

- Support for the proposal to clarify the linkage between professional skepticism and the fundamental principles/independence through additional application material in the IESBA Code of Ethics.
- In relation to the proposed text related to “critical mindset”:
  - It was not clear what problem the proposals regarding a “critical mindset” are attempting to fix.
  - It was noted that the use of the word “mindset” makes a very close link to the “questioning mind” wording in the definition of professional skepticism within the ISAs and instead suggested alternative terms such as “critical thinking.”
  - Given that the term “critical mindset” is a new concept, it is difficult to foresee how it will change auditor behavior, especially for professional accountants in business. It was also noted that there was a risk of unintended consequences.

Prof. Schilder thanked Mr. Fleck for taking steps to be responsive to the feedback provided to him by the IAASB at its September meeting. He summarized the feedback from the board in two ways:

- Generally, the Board members felt the concept was interesting, but struggled to understand what is meant, and expected, by the concept of “critical mindset”; and

- Board members questioned how this concept is different from professional skepticism and how the two terms would be reconciled.

Prof. Schilder closed the session by requesting that Mr. Fleck ask the IESBA to consider sharing a fatal-flaw review of the exposure draft with the full PSWG following the IESBA meeting, prior to its finalization. Mr. Fleck agreed to ask the IESBA to consider this.

#### WAY FORWARD

The PSWG intends to continue to progress the stakeholder communication publication and update the Board at future meetings.

### **10. ISA 315 (Revised)**

Ms. Campbell provided the Board with an overview of Agenda Item 10-A, including a summary of the outreach performed by the ISA 315 (Revised) Task Force since the IAASB's September 2016 meeting. Ms. Campbell highlighted that the SMP Committee, in a letter to the IAASB Chairman, expressed support for many of the ISA 315 (Revised) Task Force's recommendations. The SMP Committee did however express concern regarding potential unintended consequences of adding susceptibility to fraud as an additional qualitative inherent risk factor and expressed the view that the concept of "difficult for the entity to control" should not be included in a revised definition of significant risk, noting a preference that this concept be incorporated into application material to assist in explaining the nature of a significant risk.

The Board expressed support for many of the ISA 315 (Revised) Task Force's recommendations included in Agenda Item 10-A, including support for efforts to consider the ability of ISA 315 (Revised) to be applied to a wide range of circumstances and scalability with respect to the components of internal control. The Board provided additional matters for the ISA 315 (Revised) Task Force to consider as it progresses the project and in certain areas asked the ISA 315 (Revised) Task Force to consider additional points. Specifically, the Board:

- Asked the ISA 315 (Revised) Task Force to provide clarity as to how some of the proposals would be operationalized, particularly the recommendation to require the auditor to develop an expectation of the classes of transactions, account balances and disclosures expected to be in the entity's financial statements and the consideration of the qualitative inherent risk factors in the identification of significant risks.
- Suggested that the ISA 315 (Revised) Task Force continue to explore the implications of a combined or separate assessment of inherent risk and control risk.
- Recommended outreach with the PCAOB regarding the proposal to require the auditor to determine significant classes of transactions, account balances and disclosures, and their relevant assertions, to further understand how this is applied in practice.
- Expressed mixed views regarding the ISA 315 (Revised) Task Force's recommendations related to paragraph 18 of ISA 330 to change the requirement for substantive procedures from 'material' classes of transactions, account balances and disclosures to those that are 'significant'. Board members noted variously that the recommendations may result in the purpose of that paragraph being completely different than what is currently intended.
- Expressed mixed views regarding adding the susceptibility to fraud as an additional qualitative inherent risk factor, with some expressing support as being a needed addition, while others noted the

risk of confusion regarding the extent of the consideration of controls related to inherent risks (as certain aspects of fraud, such as opportunity, relate to consideration of controls).

- Asked the ISA 315 (Revised) Task Force to further consider and clarify the interactions between the qualitative inherent risk factors being proposed for ISA 315 (Revised) and the qualitative factors noted within the ISA 540 project.
- In relation to the Task Force recommendation that the determination of significant risk should be based on the relative likelihood and magnitude of misstatement, and on the nature of the risk in the context of the qualitative inherent risk factors (i.e., a high inherent risk driven by the relative likelihood and magnitude of misstatement and one or a combination of the qualitative inherent risks factors), whether a definition of significant risk that includes these concepts would sufficiently facilitate the auditor's determination of significant risks given these concepts are relevant to the assessment of all inherent risks;
- Queried whether those inherent risks that have a low likelihood of misstatement, but if that misstatement were to occur, it would be of high magnitude in terms of its materiality, would be considered to be a significant risk;
- Provided various suggestions for the ISA 315 (Revised) Task Force to consider related to the definition of significant risk, including that:
  - Significant risk should remain a subset of inherent risks; and
  - Reference to "difficult for management to control" be considered for application material and not within the definition or the requirements.

#### PIOB OBSERVER REMARKS

Prof. Van Hulle commented on the addition of susceptibility to fraud as a qualitative inherent risk factor, noting that from a public interest perspective there is an expectation that the susceptibility of fraud be a part of the auditor's considerations in the identification and assessment of risks.

#### WAY FORWARD

The ISA 315 (Revised) Task Force will continue to progress possible changes to ISA 315 (Revised), taking into account the Board's feedback. The ISA 315 (Revised) Task Force will bring further matters for discussion to the March 2017 CAG and IAASB meetings on issues identified in the project proposal that have not yet been discussed such as matters related to information technology, data analytics and professional skepticism in the context of the auditor's risk assessment procedures.

#### **11. International Accounting Standards Board (IASB) Annual Review**

Prof. Schilder and Mr. Blascos, Chair of the IAASB-IASB Liaison Working Group, welcomed IASB Member Ms. Mary Tokar to the IAASB meeting. Ms. Tokar updated the Board on the IASB's work plan, and provided an overview of the significant projects of the IASB that are in progress (disclosures, primary financial statements and materiality), as well as the projects recently completed by the IASB that are expected to

impact auditors (revenue recognition,<sup>14</sup> financial instruments<sup>15</sup>, leases<sup>16</sup> and insurance<sup>17</sup>). Ms. Tokar described the feedback received from respondents on the IASB's recent Agenda Consultation and explained the IASB's work on Alternative Performance Measures. Ms. Tokar emphasized the need for improving communication in financial reporting and supporting the implementation and application of the International Financial Reporting Standards.

## **12. Closing Remarks from IAASB CAG Chairman**

Mr. Waldron was of the view that the IAASB meeting was successful and he thanked the Board for their support.

## **13. PIOB Observer Remarks**

Prof. Van Hulle was supportive of the Board's efforts and announced that Charles (Chuck) Horstmann has resigned from the PIOB. He further explained that the PIOB has resolved to organize the observations of the meetings of the standard setting boards in a more structured, coordinated way and, accordingly, the PIOB will assign a team that will be responsible for observing the meetings in respect of each standard setting board. Prof. Van Hulle noted that Mr. Holm and himself would be observing the IAASB board meetings in 2017.

## **14. Next Meeting**

The next IAASB Teleconference will be held on January 31, 2017. The next IAASB physical meeting will be March 13–17, 2017, to be held in Lima, Peru.

## **15. Closing**

Ms. Bahlmann noted the IAASB meetings and teleconference calls for 2017, as well as the upcoming CAG meetings and outreach activities.

Prof. Schilder thanked the Board Members, the Technical Advisors and the IAASB staff for the hard work on the different topics discussed during the week and congratulated the Board on the results that have been achieved.

Prof. Schilder then closed the meeting.

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<sup>14</sup> IFRS 15, *Revenue from Contracts with Customers*

<sup>15</sup> IFRS 9, *Financial Instruments*

<sup>16</sup> IFRS 16, *Leases*

<sup>17</sup> IFRS 4, *Insurance Contracts*