



## **Public interest issues under current PIOB scrutiny: IAASB projects**

**February 2018**

In response to our undertaking to communicate the public interest issues more clearly that are a concern to the PIOB, we set out below a list of the public interest issues in current IAASB projects identified from observation activities by our members and from analyses carried out by our staff. The purpose of this communication is to share with the SSB the public interest concerns the PIOB may have at this stage of the relevant project's development. Most of these concerns have already been raised by PIOB observers at meetings. It is acknowledged that each of the projects identified below is work-in-progress and that further deliberation and refinement are ongoing. Consequently, the list below is not exhaustive, and does not preclude the PIOB from raising further issues in the future.

In the context of IAASB projects, the topics of particular interest of a public interest nature at this time are ISA 540; ISQC1; ISA 315; and Professional Skepticism.



Public Interest Oversight Board

ISA 540	
PIOB public interest Concern	Description of the PIOB concern
<b>Better explanation and articulation of risk factors</b>	The risk factors (RF) need to be clearly explained and articulated in the standard, and well supported by application material.
<b>Requirement to understand and test internal controls</b>	Auditors should thoroughly understand and test the internal controls around complex accounting estimates and valuation models, particularly for financial institutions. A robust internal control environment is a critical part of an entity’s governance system; including how risk is managed by the entity and reported in the entity's financial statements.
<b>Additional ECL-specific application material should be included in ISA 540</b>	Given that ISA 540 applies to all accounting estimates, additional guidance on auditing complex ECL estimates and valuation models would be helpful for auditors in the banking and insurance industry. Such guidance would help auditors: <ul style="list-style-type: none"> <li>• understand the entity’s business model</li> <li>• assess the classification and nature of financial assets and liabilities</li> <li>• audit management’s assessment of credit risk and the consequent accounting estimation, e.g., in “lifetime” ECLs</li> </ul>
<b>Auditors should know the applicable regulatory and prudential requirements and practices, relevant to accounting estimations – Communication with supervisors</b>	In addition to “understand regulatory factors”, auditors should be required to provide evidence that the financial institutions comply with the applicable prudential requirements and practices, relevant to accounting estimates.  Auditors of financial institutions should be required to communicate regularly with supervisors on key issues.
<b>Early adoption</b>	Given the length in the development of this standard, the PIOB supports early adoption of the ISA by auditors.



<b>ISQC 1 – QUALITY CONTROL AT THE FIRM’S LEVEL</b>	
<b>The firm’s business model (BM) should not interfere with audit quality (AQ)</b>	The audit firm's BM should promote good AQ. This is especially important when non-audit services (NAS) are being delivered in the context of an audit. The BM includes the governance structure of the firm; adherence to ethical requirements by the firm’s management and by the auditors; and auditor’s accountability.
<b>Networks need to be addressed in ISQC1</b>	Investors and those who use audit services from a global “branded firm” should receive uniform quality from that brand. Requirements at the Network level are needed in ISQC1, e.g.; QMS should be set at the network level; as well as quality control, internal inspections, and quality control monitoring.
<b>ISQC1 should highlight the public interest role of the audit</b>	The public interest role played by an auditor should be highlighted in ISQC1. This could be done by reminding firms/auditors that high quality audits are in the public interest.
<b>Transparency Reports (TR) should be required in ISQC1</b>	ISQC 1 should require audit firms to publish TR. Communicating externally the firm’s quality systems is in the public interest. This would include a firm’s operating practices; corporate governance structures; audit and non-audit professional services and related fees; remuneration schemes and incentives for partners; and the firms’ quality management system. TR are already required in the EU as well as in other jurisdictions; and in others, they are voluntarily provided by some firms.
<b>The objective of a QMS should focus on high quality audits</b>	The current objective is too compliance-oriented and is not aligned with the objectives of the new QMS. Compliance is a way to achieve quality, but not an end in itself. The objective should be reformulated to reflect that “achieving high audit quality” is the priority of any QMS.
<b>Professional Skepticism (PS) needs to be included in ISQC1</b>	ISQC1 should highlight the direct link between PS and AQ. ISQC 1 should also include the main risks to PS, namely, the firm's commercial dependency on the client; the firms' business model; and issues around auditor independence.
<b>The IAASB should continue coordinating with the IESBA aspects related to ethical requirements</b>	The IAASB should continue coordinating with the IESBA those aspects that link to ethics, e.g., ethical requirements, auditor independence, and engagement quality control reviews. Topics regulated by the IESBA Code of Ethics, e.g., cooling off periods, should be the same in the IAASB standards. ISQC1 could highlight that NOCLAR, conflicts of interest, and the provision of non-assurance services constitute risks to AQ.



Public Interest Oversight Board

<p><b>Engagement Quality Control Reviews (EQCRs) should be required for all PIEs</b></p>	<p>EQCRs are currently required in ISQC 1 for listed entities only.</p>
<p><b>ISA 315, “Identifying and assessing the risk of material misstatement, through understanding the entity and its environment”</b></p>	
<p><b>Risk Assessment Procedures Need to be Strengthened</b></p>	<p>The identification of risks of material misstatement is at the core of any risk-based audit and is the starting point for auditors to design the procedures that will address those risks. The standard needs to acknowledge the impact of technology on audit procedures (e.g.; big data; data analytics; cyber risks and cyber security); include the importance of professional scepticism; and update the risk factors.</p>
<p><b>Susceptibility to fraud (STF) should be included as a risk factor in the standard</b></p>	<p>STF should be one of the risk factors included in ISA 315, given that this is clearly a public interest issue; in addition to the other factors being discussed by the IAASB.</p>
<p><b>Separate assessments for inherent risks and control risks</b></p>	<p>The PIOB supports a separate identification and assessment of inherent risks and control risks in ISA 315. This would allow auditors to better design their procedures for each type of risk.</p>
<p><b>Procedures around internal controls should be updated</b></p>	<p>Auditor’s work and conclusions over an entity’s internal controls need to be strengthened in ISA 315, for instance by acknowledging the impact of technological change.</p>
<p><b>Professional Skepticism (PS)</b></p>	
<p><b>Strengthening PS in the ISAs</b></p>	<p>At the time of the “Invitation to Comment”, the PIOB recommended the IAASB pay attention to PS, because it relates to going concern, auditor independence, and management bias. The PIOB also highlighted the need to consider how auditors should document PS and looks forward to the IAASB’s strengthening the notion of PS throughout the standards.</p> <p>The PIOB supports PS to apply to all accountants and auditors. Auditors may have different requirements around PS.</p>