

December 31, 2007

Mr. James Sylph
 Technical Director, IAASB
 International Federation of Accountants
 545 Fifth Avenue, 14th Floor
 New York, NY 10017

Re: Exposure Drafts: *Proposed Redrafted International Quality Control Standard 1, Quality Control for Firms that Perform Audits and Reviews of Financial Statements, and Other Assurance and Related Services Engagements, and International Standard on Auditing (ISA) 220 (Redrafted), Quality Control for an Audit of Financial Statements.*

Dear Mr. Sylph:

The American Institute of Certified Public Accountants (AICPA) is pleased to comment on the above referenced exposure draft. We commend the International Auditing and Assurance Standards Board (IAASB) on its proposed revisions to International Standard on Auditing (ISA) 220, *Quality Control for an Audit of Financial Statements*, and International Quality Control Standard 1, *Quality Control for Firms that Perform Audits and Reviews of Financial Statements, and Other Assurance and Related Services Engagements*,

Suggested new language is shown in boldface; suggested deleted language is shown by strikethrough.

Responses to Questions for Respondents

Q1. *Are the objectives to be achieved by the auditor, stated in the proposed redrafted standards, appropriate?*

We believe that the objective stated in ISQC1 is appropriate. However, we are concerned with the inclusion of the phrase “through implementation of appropriate quality control procedures at the engagement level” in the objective of ISA 220. Engagement personnel may fail to perform appropriate quality control procedures for an audit yet still comply with all other professional auditing standards and regulatory, legal and relevant ethical requirements. But, because appropriate quality control procedures were not performed for the engagement, engagement personnel may be accused of failing to perform an audit in accordance with the ISAs, the disclaimer in paragraph A22 notwithstanding. We recommend the following revision:

“ The objective of the auditor is to obtain reasonable assurance that the audit complies with professional standards and regulatory and legal requirements, ~~through the implementation.~~ **Performance** of appropriate quality control procedures at the engagement level **assists the auditor in obtaining reasonable assurance.**”

Q2. *Have the criteria identified by the IAASB for determining whether a requirement should be specified been applied appropriately and consistently, such that the resulting requirements promote consistency in performance and the use of professional judgment by auditors?*

We believe that the criteria for determining whether a requirement should be specified have been applied appropriately and consistently except as noted below.

The following are recommended changes to the standards related to substantive issues, and an appendix containing other recommendations.

Recommended Changes Related to Substantive Issues
Comments Relating to Both Standards:

Date of Completion of Engagement Quality Control Review

Extant ISA 220 and ISQC1 require that the engagement quality control review be completed before the report is issued. The Exposure Draft changes this to require that the engagement quality control review be completed before the date of the auditor's report, and removes references to the issuance of the auditor's report as it is a term that is undefined in the *Handbook of International Auditing, Assurance, and Ethics Pronouncements*.

We believe that an engagement quality control review is an objective review of the audit evidence and the conclusions reached by the engagement team. The quality control review itself does not obtain or provide sufficient appropriate audit evidence for audit engagements. We acknowledge that an engagement quality control review may identify instances where additional audit procedures are needed or additional evidence is required that would necessitate the date of the auditor's report being changed to the date when sufficient appropriate audit evidence is obtained. Accordingly, we believe that the engagement quality control review does not need to be completed before the date of the auditor's report, but that the requirement should be for completion of the engagement quality control review before the report is issued. We recommend that the report issuance date be defined as "the date the auditor grants the entity permission to use the auditor's report in connection with the financial statements", and that the definition be included in the *Handbook of International Auditing, Assurance, and Ethics Pronouncements*.

Comments on Exposure Draft: Proposed Redrafted International Standard on Auditing 220, Quality Control for an Audit of Financial Statements

We are concerned that this standard imposes requirements on engagement partners that are firm-level responsibilities. Specifically, the requirement in paragraph 8 for the partner to evaluate whether members of the engagement team have complied with relevant ethical requirements will be difficult to operationalize in large firms. In addition, if one is required to remain alert, to be required to observe is redundant. We suggest the following revision:

8. The engagement partner shall ~~evaluate whether members of the engagement team have complied with relevant ethical requirements:~~
- ~~(a) Through inquiry and observation regarding ethical matters among the engagement team as necessary throughout the audit engagement, and~~
 - ~~(b) By remaining alert,~~ **through observation and inquiry as necessary,** for evidence of non-compliance with ~~these~~ **relevant ethical** requirements **by members of the engagement team throughout the audit engagement.**

Paragraph 11 We are concerned that the requirement to be satisfied that appropriate procedures have been followed leaves auditors open to charges of failing to perform an audit in accordance with the ISAs if a procedure in the firm's client acceptance and continuance process is inadvertently omitted or if the firm's quality control procedures in this regard have deficiencies. We believe that the engagement partner should be able to place reliance on the firm's systems. We suggest the following revision:

11. The engagement partner shall **consider information obtained from the firm's process** ~~be satisfied that appropriate procedures regarding the~~ of acceptance and continuance of client relationships and shall ~~determine that conclusions reached in this regard are appropriate~~ **be satisfied that an audit in accordance with professional standards and regulatory and legal requirements can be performed, and that an auditors' report that is appropriate in the circumstances can be issued.**

Comments on Exposure Draft: Proposed Redrafted International Quality Control Standard 1, Quality Control for Firms that Perform Audits and Reviews of Financial Statements, and Other Assurance and Related Services Engagements

- Paragraph 17 We believe the requirement regarding the content of the communication, and the requirement to encourage personnel to communicate their views, are overly prescriptive and should be moved to application material.
- Paragraphs 29, A8-A10 The familiarity threat is one of several threats to independence discussed in the IFAC Code. We question why only the familiarity threat is singled out for additional requirements. We believe that this appears to minimize the importance of the other threats to independence, and we recommend that the standard address all the threats to independence, individually or collectively.
- Paragraph 30 We believe that it is important for firms to consider all the risks, in addition to those risks rising from a client's lack of integrity, associated with providing professional services. We recommend the following revision:

30. ...that it will ~~only~~ undertake or continue relationships and engagements **only** where the firm:
(a) Has considered the integrity of the client, including the identity and business reputation of the client's principal owners, key management, related parties and those charged with its governance, and ~~does not have information that would lead it to conclude that the client lacks integrity~~ **the risks associated with providing professional services in the particular circumstances;**
- We believe that obtaining an understanding with the client regarding the nature, scope, and limitations of services to be performed minimizes the risk of misunderstandings regarding those services. ISA 210, *Terms of Audit Engagements*, requires obtaining this understanding and documenting it in an engagement letter or other form of contract, for audit engagements. We believe that obtaining this understanding is of sufficient importance to warrant being a requirement for all engagements. We recommend the inclusion of application material noting that whether the understanding may be oral or should be written is dependent on the nature of the engagement.
- Paragraphs 40 and A34 We believe that consultation can be effective only when all the relevant facts known to the engagement team are provided to those consulted. We recommend that this be elevated from application material to a requirement.
- We believe that inspection is only one element of monitoring, and that the need for and extent of inspection procedures depends on the existence and effectiveness of the other monitoring procedures. In the US, regulators require of licensees, and the AICPA requires of its members, participation in a peer review program. We believe that these requirements meet the intent of the requirement for inspections, and

accordingly, Statement on Quality Control Standards (SQCS) No. 7, *A Firm's System of Quality Control*, does not require inspections. We believe that ISQC1 should allow member bodies, working with their regulators, to determine whether requiring inspections is necessary in their jurisdictions.

We recommend that the requirement in paragraphs 55(a) and 56 be moved to application material, and that the following additional guidance be provided:

Inspection procedures with respect to the engagement performance element of a quality control system are particularly appropriate in a firm with more than a limited number of management-level individuals responsible for the conduct of its accounting and auditing practice.

- Paragraph 55(c) and A64 We agree that in small firms, monitoring procedures may need to be performed by some of the same individuals who are responsible for compliance with the firm's quality control policies and procedures, or who may be involved in performing the engagement quality control review. This is the case in the United States, and our peer review process, which also provides a safeguard of external inspections on a cyclical basis, has evidenced that monitoring procedures can be effective in these circumstances. We believe that if sole practitioners are capable of implementing effective quality control systems, including reviewing their own work on engagements and obtaining reasonable assurance that the reports issued by the practitioner are appropriate in the circumstances, then they should have the option of monitoring their quality systems. SQCS No. 7 allows small firms this flexibility, and accordingly we suggest the following revisions to ISQC1 paragraphs 55(c) and A64:

55. (c) ~~Require that those performing the engagement or the engagement quality control review are not involved in inspecting the engagements~~ **Assign performance of monitoring of the firm's system of quality control to qualified individuals.**

A64. In the case of small firms **with a limited number of persons with sufficient and appropriate experience and authority in the firm**, monitoring procedures may need to be performed by **some of the same** individuals who are responsible for ~~design and implementation of~~ **compliance with** the firm's quality control policies and procedures, or who may be involved in performing the engagement quality control review. **To effectively monitor one's own compliance with the firm's policies and procedures, it is necessary that an individual be able to critically review his or her own performance, assess his or her own strengths and weaknesses, and maintain an attitude of continual improvement. Changes in conditions and in the environment within the firm (such as obtaining clients in an industry not previously serviced or significantly changing the size of the firm) may indicate the need to have quality control policies and procedures monitored by another qualified individual. Having an individual inspect his or her own compliance with a quality control system may be less effective than having such compliance inspected by another qualified individual. When one individual inspects his or her own compliance, the firm has a higher risk that noncompliance with policies and procedures will not be detected. Accordingly, a** A firm with a limited number of persons may choose to use a suitably qualified external person or another firm to carry out engagement inspections and other monitoring procedures. Alternatively, they may wish to establish arrangements to share resources with other appropriate organizations to facilitate monitoring activities.

- We believe that firms may consider whether firm personnel can effectively gain the necessary knowledge of relevant industries or subject matters when considering whether to undertake a new engagement from a new or existing client. Accordingly, we suggest the following revisions:

A15. ...• Firm personnel have knowledge of relevant industries or subject matters **or the ability to effectively gain the necessary knowledge;**

A17. ...For example, a client may have started to expand its business operations into an area where the firm does not possess, **and cannot effectively gain,** the necessary knowledge or expertise.

- Paragraph A18 Paragraph 33 requires documentation of identified issues when a firm decides to accept an engagement. We believe that it is equally important to document the issues identified when a firm decides to withdraw from an engagement or both the engagement and the client relationship, and therefore recommend that the documentation of significant matters, consultations, conclusions and the basis for those conclusions included in application material be elevated to a requirement.
- Paragraph A43 It is not clear what is meant by “consultation is a necessary part of the engagement partner’s process”. Does this mean that the engagement partner must reach a conclusion before consulting the engagement quality control reviewer, so that the engagement quality control reviewer’s opinion is not “necessary”? Or does it mean that when the engagement partner is in a situation where consultation on an issue is required, the engagement quality control reviewer is not the appropriate person with whom to consult? If so, we recommend the following revision:

“...However, when the ~~consultation is a necessary part of the engagement partner’s~~ **firm’s policies and procedures require the engagement partner to seek consultation as part of the** process of forming an opinion on a matter, consultation with the engagement quality control reviewer for this purpose would not be appropriate.

Thank you for the opportunity to comment on this exposure draft. If you have any questions regarding the comments in this letter, please contact Ahava Goldman at +1-212-596-6056, agoldman@aicpa.org or Sharon Walker at +1-212-596-6026, swalker@aicpa.org.

Respectfully submitted,



/s/ Harold Monk, Jr.
Chair, Auditing Standards Board

Appendix: Other Recommendations

Applicable to Both Exposure Draft: *Proposed Redrafted International Standard on Auditing 220, Quality Control for an Audit of Financial Statements* and Exposure Draft: *Proposed Redrafted International Quality Control Standard 1, Quality Control for Firms that Perform Audits and Reviews of Financial Statements, and Other Assurance and Related Services Engagements*

- To be consistent with the wording in ISQC1 paragraphs 35, 37 and 38, and with the use of the active voice in ISQC1 paragraph 11(a), we recommend the following change to ISQC1 paragraphs 11 and 57:

11 (b) — ~~Reports issued by the firm or engagement partners~~ **issue reports that** are appropriate in the circumstances.

57. (a) Instances that do not necessarily indicate that the firm's system of quality control is insufficient to provide it with reasonable assurance that it complies with professional standards and regulatory and legal requirements, and that the ~~reports issued by the firm or engagement partners~~ **issue reports that** are appropriate in the circumstances;

Accordingly, we also recommend the following change to ISA 220 paragraph 2(b):

2 (b) — ~~Reports issued by the firm or engagement partners~~ **issue reports that** are appropriate in the circumstances.

- The distinction between a “qualified external person” and a “suitably qualified external person” is not apparent. Because eliminating superfluous words enhances clarity, we recommend deleting the modifier “suitably” in all instances in which it appears in these standards.
- In the interest of brevity, we recommend deleting the repetition of the definition of engagement quality control review from the definition of the engagement quality control reviewer in ISA 220 paragraph 6(c) and ISQC1 paragraph 12(d) as follows.

Engagement quality control reviewer – A partner, other person in the firm, ~~suitably~~ qualified external person, or a team made up of such individuals, none of whom is part of the engagement team, with sufficient and appropriate experience and authority to ~~objectively evaluate the significant judgments the engagement team made and the conclusions they reached in formulating the report~~ **perform the engagement quality control review.**

- Although it can be argued that national requirements that are less restrictive are not relevant because they are rendered moot by the more restrictive requirements of the IFAC code, national requirements that are less restrictive are still requirements to which the engagement team and engagement quality control reviewer are subject. Thus we recommend the following revision to ISA 220 paragraph 6(r) and ISQC1 paragraph 12(p):

...national requirements, ~~that are~~ **which may be** more restrictive.

- Because the term partner is also used to denote a form of ownership, we recommend adding the following to the definition of partner in ISA 220 paragraph 6(k) and ISQC1 paragraph 12(l)

For purposes of this definition, partner may include an employee with this authority who has not assumed the risks and benefits of ownership. Firms may use different titles to refer to individuals with this authority.

- The wording in ISA 220 paragraph 15 and ISQC1 paragraph 39 precludes having equally experienced team members review each other's work. In addition, a team member with fewer years experience may nonetheless be more knowledgeable in a subject matter, but "more experienced" may not be interpreted to cover these situations. We suggest the following:

... shall be determined on the basis that ~~the work of a less experienced team member is reviewed on a timely basis by a more experienced engagement team member.~~ **qualified engagement team members, which may include the engagement partner, review work performed by other team members on a timely basis.**

- The application material in ISA 220 paragraph A12 and ISQC1 paragraph A31 can readily be adapted into a checklist for review procedures. Ideally, the questions in a checklist are worded so that when things are as expected, the answers are all the same – that is, every question can be answered as a yes. The list meets this best practice with the exception of the fourth bullet – "There is a need to revise the nature, timing and extent of work performed;". Unlike the other items in this list, the expected answer to this would be no. We suggest "There is a need to revise the nature, timing and extent of work performed **are appropriate and without need for revision**"

Other Recommendations on Exposure Draft: *Proposed Redrafted International Standard on Auditing 220, Quality Control for an Audit of Financial Statements* ISA

- The relationship between paragraph 3, which discusses the role and entitlement of engagement teams, and the rest of the ISA is not clear. In extant ISA 220, this paragraph clearly relates to the extant requirement in paragraph 2 for engagement teams to implement quality control procedures. The concepts regarding engagement teams are important and should be retained, but the paragraph needs to be better integrated into the ISA. Adding a title to the paragraph may achieve this.

Other Recommendations on Exposure Draft: *Proposed Redrafted International Quality Control Standard 1, Quality Control for Firms that Perform Audits and Reviews of Financial Statements, and Other Assurance and Related Services Engagements*

- Paragraphs 19, 23, and 61 For the sake of brevity, we suggest the following revision:

19. ... Such policies and procedures shall require the firm's **leadership** (chief executive officer (or equivalent) or, if appropriate, the firm's managing board of partners (or equivalent)),...

23. Any person or persons assigned operational responsibility for the firm's quality control system by the firm's ~~chief executive officer or, if appropriate, its managing board of partners~~ **leadership** ...

61. At least annually, the firm shall communicate the results of the monitoring of its quality control system to engagement partners and other appropriate individuals within the firm, including the firm's ~~chief executive officer or, if appropriate, its managing board of partners~~ **leadership**.

- Paragraph A3 can be deleted and its concepts incorporated into paragraph 23, as follows. We believe this will clarify the intent of the requirement in paragraph 23, as well as shorten the standard and put all related concepts in one paragraph.

23. ...have sufficient and appropriate experience and ability; **to identify and understand quality control issues and to develop appropriate policies and procedures, as well as** the necessary authority ~~to assume that responsibility.~~ (Ref: ~~Para. A3~~) **to implement those policies and procedures.**

- Paragraph 35 The phrase “regarding assessment of its staff’s capabilities and competencies” is superfluous and, because the objective is to have sufficient personnel and personnel is defined as partners and staff, potentially confusing. We recommend deleting this phrase.
- Paragraph 46(b) and 47 Because the degree to which an engagement quality control reviewer can be consulted relates more to the reviewer’s objectivity than to the reviewer’s eligibility for appointment, we suggest the following revision:

46. The firm shall establish policies and procedures to address the appointment of engagement quality control reviewers and establish their eligibility through:

~~(a) The~~ **the** technical qualifications required to perform the role, including the necessary experience and authority. ~~and;~~ (Ref: Para. A42)

~~(b) The degree to which an engagement quality control reviewer can be consulted on the engagement without compromising the reviewer’s objectivity,~~ (Ref: Para. A43)

47. The firm shall establish policies and procedures designed to maintain the objectivity of the engagement quality control reviewer, **including the degree to which an engagement quality control reviewer can be consulted on the engagement without compromising the reviewer’s objectivity.** (Ref: Para. ~~A44~~**A43**-A47)

- Paragraphs 52, A50 To more concisely convey the material, we suggest the following revisions:

52. ... assembly of final engagement files on a timely basis after the engagement reports have been ~~finalized~~ **issued.**

A50....Where no such time limits are prescribed in law or regulation, ~~paragraph 55 requires the firm to~~ **the time limits established in the firm’s** policies and procedures related to time limits that reflect the need to complete the assembly of final engagement files on a timely basis **will depend on the nature of the engagement.**

- Paragraph A23 We suggest adding the word “Effective” at the beginning of the paragraph to make the first sentence true in all instances. Also, we recommend adding the concept of compensation to the third bullet, because compensation should also depend, among other things, on the matters noted, and to provide some guidance regarding compensation. Suggested wording is as follows:

“Helping personnel understand that **their compensation and** advancement...”

- Paragraph A25 The language is stilted. We suggest “The firm may use a ~~suitably~~ qualified external person, for **example** when internal technical and training resources are unavailable, ~~or for any other reason.~~”

- Paragraph A53 We are concerned that the sequence “created, changed or reviewed” in the first bullet of may lead people to believe that if documentation is begun on one date and completed over the course of several days all those dates would need to be documented. We suggest revising the sequence to “created, ~~changed or reviewed~~ **or changed.**”

- Paragraph A32 The last phrase “to resolve a difficult or contentious matter” is superfluous.
- Paragraph A43 To be consistent with the wording in paragraph 47, we suggest that the words “compromise” and “compromised” in paragraph A43 be replaced with the words “impair” and “impaired”.
- Paragraph A54 In the first bullet, we suggest “data encryption” in addition, or as an alternative, to passwords.
- Paragraph A55 Since the legal, regulatory or other reasons for a firm to retain original paper documentation may apply whether or not the documentation has been scanned, to clarify the final sentence we suggest ~~“There may be~~ **Original paper documentation that has been scanned may need to be retained** for legal, regulatory, or other reasons ~~for a firm to retain original paper documentation that has been scanned”~~.
- To avoid confusion, the use of present tense in the application material pertaining to firm actions should be avoided. We suggest the following revisions, including the deletion of superfluous text in paragraph A58:

Paragraphs A15 and A27 “the firm **may** considers”

Paragraph A28 ~~“The firm~~ **Effective policies and procedures** promotes consistency in the quality of engagement performance ~~through its policies and procedures.”~~

Paragraph A58 “Procedures that the firm **may** adopts for retention of engagement documentation include those that ~~enable the requirements of paragraph 54 to be met during the retention period”~~.
- Paragraph A55 It is not clear whether the procedures described are required to be followed in all instances when original paper documentation is electronically scanned, in which case a conditional requirement has been included in application material. To clarify, we suggest the following revision:

“...In such cases, the firm’s procedures designed to maintain the integrity, accessibility, and retrievability of the documentation ~~would~~ **may** include...”