

13 May 2016

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Dear Mdm,

RESPONSE TO THE INTERNATIONAL AUDITING AND ASSURANCE STANDARDS BOARD (IAASB) INVITATION TO COMMENT, *ENHANCING AUDIT QUALITY IN THE PUBLIC INTEREST: A FOCUS ON PROFESSIONAL SCEPTICISM, QUALITY CONTROL AND GROUP AUDITS* (ITC).

The Institute of Singapore Chartered Accountants (ISCA) commends the IAASB's efforts in enhancing the International Standards on Auditing (ISAs) and the International Standard of Quality Control (ISQC) 1 to advocate audit quality and remain relevant to the profession.

To solicit meaningful feedback for this important project, ISCA undertook the following initiatives to seek views from key stakeholders:

- (i) Conducted a one-month public consultation to seek feedback from its members;
- (ii) Organised a number of focus groups to engage diversified key stakeholders, including the preparers of financial statements, directors and those charged with governance, audit firms, academics, regulators and public agencies, to obtain their views on the proposals in the ITC; and
- (iii) Discussed the ITC with members of the ISCA Auditing and Assurance Standards Committee.

Executive Summary

Generally, our key stakeholders were of the opinion that introducing more rules within the auditing standards would not be necessary as the existing standards are sufficiently robust. Audit professionals should be left to exercise their judgement when designing audit procedures and determining what constitutes sufficient appropriate audit evidence.

Notwithstanding the above, the stakeholders welcome more practical guidance materials from the IAASB on the three topics in the ITC.

In addition, the stakeholders were strongly of the view that since audit professionals are bound by a stringent ethics code and the work carried out by them has to adhere to one of the frameworks under the auditing and assurance standards, the audit profession is capable of doing the right things such as enhancing audit quality. Using remuneration as a means to promote audit quality amongst the profession may not be the most appropriate.

Our comments are included in our response to the selected questions in the ITC as follows:

Professional Scepticism

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

Generally, we agree with the definition that professional scepticism is an attitude with a questioning mind and being alert to unusual conditions. Auditors should commence an audit with a curious mind and scepticism should only come into play when there is a reason to believe that something is amiss. Otherwise, the word “scepticism” may connote a negative meaning.

To promote proper application of professional scepticism in practice, we would like to highlight that holistic on-the-job training to educate junior auditors on the correct mindset is critical. They ought to be trained on how to critically assess audit evidence, ask pertinent questions and determine what information they should be alerted to. In the absence of proper trainings, junior auditors may risk becoming confrontational if they approach management with an incorrect attitude. Such trainings should also reiterate and reinforce the mindset that it is part and parcel to be sceptical in an audit if it is done in good faith.

Similarly, we also believe that greater involvement and coaching by the engagement partner and manager would serve as an effective catalyst in promoting greater application of professional scepticism, via regular and robust communications between the team members.

For higher risk engagements, a step towards a more sceptical audit would be to involve industry specialists such as a forensic team, to design special audit procedures to inject an element of unpredictability and in-depth audit evidence and approach.

To better describe and illustrate the professional scepticism concept, one suggestion would be for the IAASB to develop case studies or role play scenarios that can be used as training materials for the junior auditors.

2. PS 2: What do you believe are the drivers for, and impediments to, the appropriate application of professional scepticism?

We agree that strengthening auditors' professional scepticism would improve audit quality. We believe that the key drivers for the appropriate application of professional scepticism are cultures (e.g. auditors in certain jurisdictions are more comfortable challenging management), appropriate tone from the top (e.g. audit engagement partner (including the firm) leading by example), and personality of the individual (e.g. an individual who is professionally more curious and meticulous). As defined in ISA, professional scepticism is a mindset and an attitude. Such mindset and attitude will be most effective when the audit firms inculcate such mindset and attitude into the firm's values and culture.

Conversely, immense time pressures and stringent deadlines act as major deterrents to adopting a sceptical mindset for fear of not being able to complete their client deliverables promptly. To top it off, the lack of competency and/or confidence of junior auditors to challenge management may create more barriers.

PS 2: What role should we take to enhance those drivers and address those impediments?

To address the impediments, more examples or real-life case studies of audit failures caused by the lack of application of professional scepticism would help to create awareness and be useful training materials for the auditors. Overall at the firm-level, there should be a culture of open communication, encouragement and tolerance of alternative viewpoints.

Likewise, on the use of technology in audits, we agree that it is timely to explore how data analytics could be integrated into an audit to enhance professional scepticism. Audit data analytics have and could significantly change the way audits are conducted. In addition, the profession should invest in research and development to identify new robust audit evidence. Such audit evidence may be available due to greater use of technology in commercial transactions and hence they should replace or supplement the traditional documentary audit evidence.

The IAASB, the regulators and audit oversight bodies have a pivotal role to play in encouraging the application of professional scepticism. This will provide a strong impetus for the audit firms to inculcate the proper application of professional scepticism as part of their firm culture and training for their staff.

Quality Control

The preparers of financial statements generally felt that the overall quality of audit in Singapore has improved over the years with the clarified auditing standards and increased regulatory requirements. Furthermore, with the introduction of key audit matters, the quality

of audit is set to improve with increased transparency. To continue to uphold the quality of audit, they are of the view that audit firms ought to have better talent management strategies such as attracting the right people.

ISCA would like to commend the efforts of our forward-looking regulator, the Accounting and Corporate Regulatory Authority (ACRA), who stepped up their efforts in promoting audit quality in Singapore. ACRA has introduced an Audit Quality Indicators¹ (AQIs) Disclosure Framework to enable audit committees of listed companies to better evaluate and select the right auditor. The AQI framework, the first of its kind in the region, comprises 8 comparable quality markers that correlate closely with audit quality based on ACRA's observations from inspecting auditors over the past decade. These include hours spent by senior audit team members involved in the audit, relevant experience of the senior audit team members and results from internal and external inspections of auditors.

1. QC2: Engagement Partner Roles and Responsibilities

We believe that the more immediate solution would be to address implementation issues rather than imposing more requirements in the existing standards. The standards, if revised, should not be prescriptive in nature. Engagement partners, being qualified professionals, should be allowed to think in depth and make the correct judgement call. There could be more guidance in this aspect but the onus ultimately lies with the engagement partner to exercise professional judgement rather than allowing the standards to prescribe most aspects of an audit.

Regarding a possible action to address the issue, the IAASB may wish to consider developing application materials to specifically address situations where an engagement partner is not located where the majority of the audit work is performed. Examples of such situations are (i) where the group engagement partner relies on the work of component auditor(s) or (ii) where the audit client has a shared service centre in another jurisdiction and the engagement partner needs to ask another auditor located in the shared service centre to perform the audit work. Such shared service centres are becoming increasingly prevalent with the changing business environment and rising business costs.

2. QC 6: Engagement Quality Control Reviews and Engagement Quality Control Reviewers (EQCRs)

Practitioners in Singapore felt that any new application materials developed relating to engagement quality control reviews and EQCRs should not be elevated to requirements. They are also strongly against having a separate standard for EQCRs. An engagement quality control review should be performed in accordance with a firm's risk management policy.

¹ https://www.acra.gov.sg/Publications/Guides/Audit_Quality_Indicators_Disclosure_Framework/

More specifically, the role of an EQCR should be clearly articulated in the standard to emphasise its objectivity and independence. The EQCR should be an impartial party with no interaction with the client. The engagement partner should be the one fronting the client on behalf of the engagement team. By maintaining such independence, the EQCR would then be able to make decisions without being unduly influenced by any client pressures. Accordingly, there is also no compelling reason for the EQCR to have separate communication with the audit committee. This would ensure independence and safeguard the quality of an audit.

3. QC 7: Monitoring and Remediation

We believe that it is most meaningful to consider how results from external and internal inspections interact with the internal monitoring system to identify and address the root causes. A well-rounded monitoring system should always take into account causal factors arising from lapses and deficiencies identified from all sources of review and improve upon them.

Such root cause analysis has already been practised in the ASEAN region with the ASEAN Audit Regulators Group (AARG). ACRA formed the AARG in 2011 with two fellow ASEAN audit regulators, Malaysia's Audit Oversight Board and Thailand's Securities and Exchange Commission, to foster collaboration between audit regulators and promote audit quality in the ASEAN region. The AARG discusses common issues relating to audit regulation and related key issues such as audit talent and engages with the international audit firms at a regional level. The AARG also helps other ASEAN economies to develop their independent audit regulation, for example, through audit inspection workshops for ASEAN audit regulators. In June 2015, the AARG concluded a meeting that discussed initiatives to raise audit quality and market transparency in the region.

4. QC 8: Engagement Partner Performance and Rewards Systems

An audit is a systematic and independent examination of an organisation's accounts by a professional (i.e. an auditor). An auditor is governed by the Code of Professional Conduct and Ethics which defines the five fundamental principles an auditor has to uphold to act in the public interest. The IAASB must recognise that audit is a profession with a reputation to uphold and capable of improving and upholding quality on our own. Hence, we are of the opinion that establishing a link between compensation and quality may not be the best option to enhance audit quality. Furthermore, such reward systems would not work for small and medium practices, especially sole proprietors. We believe that the non-financial repercussions (such as failing a practice monitoring review) are more severe than forgoing the rewards one would have received and would serve as a stronger deterrent.

Notwithstanding the above, we agree that a rewards system may affect an engagement partner's behaviour and a firm's culture to a certain extent. Hence, we are of the view that it should be left to the leadership of the firm to decide what the best course of action is to motivate its practice.

The IAASB may wish to commission a study to examine the correlation between compensation and quality before making any decisions in this regard.

Group Audits

Similar to our discussion above, we are of the view that ISA 600, *Special Considerations – Audits of Group Financial Statements (Including the Work of Component Auditors)* should remain principle-based rather than becoming rule-based (i.e. overly prescriptive).

1. GA 1(c): Should we further explore making reference to another auditor in an auditor's report? If yes, how does this impact the auditor's work effort?

We believe that the actions the IAASB is exploring in relation to revising ISA 600 are useful to ensure consistent application of key audit principles and improve quality of group audits. Among the actions proposed by the IAASB, we are of the view that there would not be a need to make reference to the component auditor in the group auditor's report. Furthermore, with the impending introduction of key audit matters in the auditor's report, such additional information would cloud the auditor's report without adding too much value.

To reiterate the above, the group engagement partner is ultimately responsible for the audit. Making reference to the component auditor would neither diminish his responsibility nor restrict his liability. Furthermore, information on the auditors of the group's subsidiary companies is already disclosed in the notes to the financial statements as required under the international accounting standards.

2. GA3: Communications between the Group Engagement Team and Component Auditors

We believe that there may be a need to bridge an existing expectation gap between what auditors understand and what the regulators expect. ISA 600 should therefore clarify what types of communication should be documented in an audit file.

In Singapore, ACRA has issued an Audit Practice Bulletin² on the audits of group financial statements to provide guidance and clarity on the audit procedures necessary prior to placing reliance on the work performed by component auditors, and to reiterate the need to increase the level of rigour and professional scepticism expected of the public accountant when acting as the group engagement auditor.

² [https://www.acra.gov.sg/uploadedFiles/Content/Publications/Audit_Practice_Bulletin/APB%20No%201%20of%202015%20\(final\).pdf](https://www.acra.gov.sg/uploadedFiles/Content/Publications/Audit_Practice_Bulletin/APB%20No%201%20of%202015%20(final).pdf)

To encourage knowledge sharing, the IAASB could explore an avenue to make such bulletins from different countries publicly available to one another.

3. GA4: Using the Work of Component Auditors

We believe that the primary challenge lies in using the work of component auditors in jurisdictions which do not follow international accounting standards. By the same token, using the work of component auditors in jurisdictions where there are robust audit regulators would be less of a concern than one without regulatory requirements.

To better illustrate, the IAASB could consider some form of guidance akin to the Singapore Audit Quality Indicators to assess suitability and competencies of the component auditors.

Other Comments

With regards to the use of low cost shared service centres by audit firms to perform routine audit procedures, we believe that the extent of involvement and nature of work done by these centres should be disclosed to those charged with governance to improve transparency.

Should you require any further clarification, please feel free to contact Mr Kang Wai Geat, Assistant Director, Technical Advisory and Professional Standards, or Ms Zoey Xie, Manager, Technical Advisory and Professional Standards, at ISCA via email at waigeat.kang@isca.org.sg or zoey.xie@isca.org.sg respectively.

Yours faithfully,



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