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Ms Jacinta Hanrahan
Senior Technical Manager
Accounting Professional & Ethical Standards Board
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Dear Jacinta

APES 110 REVISIONS TO EQCR REQUIREMENTS

We appreciate the opportunity to provide our comments to the APESB on the project to include provisions in APES110 Code of Ethics for Professional Accountants (including Independence Standards) to address the threats to objectivity of engagement quality reviewers (EQR's) and other appropriate reviewers.

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APESB has requested specific comments and feedback on the option of incorporating an Australian paragraph to enhance and clarify the requirement that an audit engagement partner cannot undertake the role of engagement quality reviewer for the same audit client without completing a two-year cooling-off period between the two roles.

In addition, the APESB have requested respondents to express a clear overall opinion on whether the proposed amendments, as a whole, are supported and that this opinion be supplemented by detailed comments, whether supportive or critical, on any matter.

Overall, we support the concept that the objectivity of the EQR is critical to an effective review and the proposed revisions to the Code take the appropriate steps to preserve objectivity by requiring an Engagement Partner (EP) to cool off for two years before becoming an EQR on the same client. However, the way the identification and evaluation of threats sections is

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written implies that these experienced and respected professionals cannot be trusted. The starting point seems to be that EP's and EQR's are unethical and because of that, they cannot be EQR's on each other's engagements and an EQR cannot be junior to an EP, despite being a partner with the appropriate knowledge and experience to perform the role.

We also have concerns that with the ever-increasing number of measures being implemented in pursuit of the 'perfect audit' from a quality and independence perspective, that it may in fact have the opposite effect, as recent statistics show that there is and will continue to be a decline in the number of RCA's available to perform audits.

Threats

The proposed new Section 325.6 A1 identifies various threats to the objectivity of a member in public practice appointed as an EQR that might be created. We have provided our comments on each of these below:

Threat	Comment
<p>(a) Self-interest Threat:</p> <ul style="list-style-type: none"> • Two Engagement Partners each serving as an Engagement Quality Reviewer for the other's engagement. 	<p>We acknowledge that there may be a potential threat when engagement partners serve as EQR on each other's engagements however these two people should also be considered respected and experienced professionals who are capable of demonstrating ethical behaviour in performing their roles despite this scenario occurring.</p> <p>The evaluation of threats section does not seem to address this threat nor do the suggested safeguards. From the guidance provided, there does not appear to be a viable solution to this scenario, which raises questions of how smaller practices can function and still perform audits which require an EQR.</p> <p>The lack of evaluation points and safeguards infers that this scenario is not acceptable. Is that the intention?</p> <p>In smaller firms where there are only a small number of audit partners, or even in larger firms there may be a limited number of partners with sufficient experience for example in a particular industry to perform the EQR role, this situation will be unavoidable. Is there an expectation that external reviewers should be used in this instance? The ramifications of sourcing EQR roles from outside of the firm are substantial, such as independence, qualifications, insurance, appropriate engagement letters, client confidentiality, and even if firms actively only take on clients which do not require an EQR and then circumstances change, this is additional inefficiency for the client and the</p>

	<p>auditor. All of which would make it harder for a smaller firm to engage and perform work where an EQR role is required, therefore without a suitable series of safeguards which are permissible within the standard this would appear to be a measure which will reduce the available pool of auditors.</p> <p>Based on an article in the Australian Financial Review on 12th May 2021, the number of RCA's has decreased by more than 20% in the last 4 years. In addition, 40% of current RCA's are due to reach retirement age in the next 5 years. Adding further requirements to an already highly regulated industry is likely to exacerbate the exit of auditors from the industry. At some point the scale of implementing measure after measure in pursuit of an audit of faultless quality and purest independence will outweigh retaining quality auditors such that there becomes a shortage of auditors. With less auditors available, independence and quality will be negatively impacted which is the complete opposite of what these requirements are trying to achieve.</p>
<p>(b) Self- review Threat:</p> <ul style="list-style-type: none"> • A Member serving as an Engagement Quality Reviewer on an Audit Engagement after previously serving as the Engagement Partner. 	<p>Out of all the threats identified, this one is more likely to occur even for a respected professional with many years of experience who demonstrates the utmost ethical behaviour. There is likely to be (at least) an unconscious bias by the partner moving from the EP role to the EQR role and they are less likely to demonstrate scepticism over judgments that they have previously made on the client as the EP. The proposed safeguard of an EP cooling off for two years before becoming an EQR on the same client addresses this threat.</p>
<p>(c) Familiarity Threat:</p> <ul style="list-style-type: none"> • A Member serving as an Engagement Quality Reviewer has a 'close relationship' with or is an Immediate Family member of another individual who is involved in the engagement. 	<p>How is 'close relationship' defined? The smaller the firm the "closer" the partners are likely to be. Does this mean that a partner from the same firm cannot perform the EQR role? This would not be a desirable outcome.</p> <p>Again, the safeguards section does not address a familiarity threat which infers that this threat cannot be reduced to an acceptable level. Is that the intention? Further the lack of any clear definition of what a "close relationship" means renders this proposal exceedingly challenging to address, comprehend and were it enabled, to execute effectively.</p>
<p>(d) Intimidation Threat:</p>	<p>Does this mean that the Partner In Charge "PIC" of an audit division cannot be an Engagement Partner on an engagement that</p>

<ul style="list-style-type: none"> A Member serving as an Engagement Quality Reviewer for an engagement has a direct reporting line to the partner responsible for the engagement. 	<p>requires and EQCR/EQR? Any EQCR assigned to their engagements will have a direct reporting line to them?</p> <p>In evaluating the threats, the proposed requirements advise considering the role and seniority of the individual appointed as EQR. Does this mean that junior partners cannot be EQR for more senior partners? If this is the case what constitutes junior and senior? Is it years of experience, in which case only partners from the same year of promotion could be EQR? The denial of the support of a more junior partner by a more senior partner would appear to be limiting the ability of senior partners to support junior partners in their roles. This is addressed by the cooling off period rather than by additional restrictions on partner seniority.</p> <p>The safeguards section addresses an intimidation threat by providing the example of reassigning reporting responsibilities within the firm which suggests that the most senior audit partner cannot be an EP or that an EQR cannot be junior to an EP due to the threat of intimidation. This will make allocation of engagements very difficult to keep track of, it will restrict the allocation of engagements for various partners (i.e. the most senior partner cannot be an EP and the most junior partners cannot be EQR's) and also infers that the partners involved cannot be trusted to behave ethically and professionally, respecting each other's opinions, in performing their roles.</p>
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The view taken by the proposed revisions to the Code in this ED in identifying and evaluating threats, is that EQR's and EP's are not capable of demonstrating the five ethical principles particularly where the EP is more senior than the EQR, where the partners have a close relationship, or where two engagement partners are EQR's for each other's engagements.

Suggested safeguards are not provided for self- review and familiarity threats which implies that these threats cannot be addressed with safeguards so should be avoided. The safeguards suggested for intimidation threat (ie, reassignment of reporting responsibilities) implies that the most senior audit partner/PIC of an audit division could not be an EP on an engagement that required an EQR or that an EQR cannot be junior to the EP as this will result in an intimidation threat.

Additional guidance is required in relation to evaluating self-review and familiarity threats and safeguards for these threats should also be included in the standard. The term 'close relationship' also requires clarification.

We support the view that the objectivity of EQR's is critical for a quality audit but do not support the view or inference in the ED that highly qualified, experienced and respected practitioners are incapable of performing their role as EP or EQR in accordance with the five fundamental principles of the Code based on the examples provided in the ED.

If you would like to discuss any of the comments made in our response please contact Maxine Ambrosini, Director Independence & Quality, or myself.

Yours sincerely



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