



AUDITING STANDARDS BOARD MEETING AGENDA
May 11-12, 2022
Las Vegas, NV and VideoConference (Zoom)
(Times are PDT)

Wednesday, May 11 8:30am –5:00pm		Thursday, May 12 8:30am – 4:00pm	
8:30–9:00 Agenda Item 1	Chair/AICPA Update	8:30–9:15 Agenda Item 5	Definition of PIEs Discuss Issues
9:00–10:30 Agenda Item 2	Quality Management Final Standard	9:15–10:00 Agenda Item 6	Audit Evidence Discuss Issues
<i>10:30–11:00</i>	<i>Break</i>	<i>10:00–10:30</i>	<i>Break</i>
11:00–12:00 Agenda Item 2	Quality Management Final Standard	10:30–11:30 Agenda Item 2	Quality Management Final Standard – Vote to Issue
<i>12:00–1:00</i>	<i>Lunch</i>	<i>11:30–12:30</i>	<i>Lunch</i>
1:00–1:30 Agenda Item 1	IAASB Update	12:30–2:30 Agenda Item 7	Executive Session
1:30–3:00 Agenda Item 3	Fraud Discuss Issues	<i>2:30–3:00</i>	<i>Break</i>
<i>3:00–3:30</i>	<i>Break</i>	3:00–4:00 Agenda Item 7	Executive Session
3:30-4:00	Fraud Discuss Issues		
4:00-5:00 Agenda Item 7	Executive Session		

Quality Management

Objective

To vote to issue as final the following proposed standards:

- [Proposed] Statement on Quality Management Standards (SQMS) *A Firm's System of Quality Control* ("SQMS 1")
- [Proposed] SQMS *Engagement Quality Reviews*; and ("SQMS 2")
- [Proposed] Statement on Auditing Standards (SAS) *Quality Management for an Engagement Conducted in Accordance with Generally Accepted Auditing Standards*, ("QM SAS") (collectively the "Proposed QM Standards").

Quality Management Task Forces

QM1

Sara Lord, *Chair*
Phyllis Anderson
Sherry Chesser
Kathryn Fletcher
Alan Long
Tania Sergott
Kimberly Stazyk

QM2/220

Jon Heath, *Chair*
Harry Cohen
Tom Parry
Jeff Rapaglia
Rick Reeder
Mike Westervelt

Background

The ASB discussed the comments received on the Exposure Draft at its October and December, 2021, and January 2022 meetings. The agenda materials presented for this meeting reflect the direction provided by the ASB at those meetings, as well as some suggestions from the AICPA Editorial Team to clarify the standards.

Amendments (Agenda item 2D)

The only changes suggested to the proposed amendments were to AT-C 105, paragraph 6, to make the language more consistent with SQMS 1. In addition, the proposed amendments have been revised to reflect the ASB's decision not to change the existing ability to date, but not issue, the auditor's report before the engagement quality review has been completed.

Matters for ASB Consideration

1. Documentation (SQMS No. 2, Engagement Quality Review)

Paragraph 30 of proposed SQMS No. 2 SAS, and the relevant application paragraphs, state the following:

The engagement quality reviewer should determine that the documentation of the engagement quality review is sufficient to enable an experienced practitioner, having no previous connection with the engagement, to understand the nature, timing, and extent of the procedures performed by the engagement quality reviewer and, when applicable, individuals who assisted the reviewer and to understand the conclusions reached in performing the review. The engagement quality reviewer should also determine that the documentation of the engagement quality review includes the following: (Ref: par. A52–A54)

- a. The names of the engagement quality reviewer and any individuals who assisted with the engagement quality review
- b. An identification of the engagement documentation reviewed
- c. The basis for the engagement quality reviewer's determination in accordance with paragraph 27
- d. The notifications required in accordance with paragraphs 26 and 27
- e. The date of completion of the engagement quality review

A52. The form, content, and extent of the documentation of the engagement quality review may depend on the following factors:

- The nature and complexity of the engagement
 - The nature of the entity
 - The nature and complexity of the matters subject to the engagement quality review
 - The extent of the engagement documentation reviewed

A53. The performance and notification of the completion of the engagement quality review may be documented in a number of ways. For example, the engagement quality reviewer may document the review of engagement documentation electronically in the IT application for the performance of the engagement. Alternatively, the engagement quality reviewer may document the review through means of a memorandum. The engagement quality reviewer's procedures may also be documented in other ways, for example, in the minutes of the engagement team's discussions when the engagement quality reviewer was present.

The GAO has requested that the first sentence of paragraph 30 be deleted because it appears to raise the EQR documentation requirement to a higher level of importance than may have been intended. As written, paragraph 30 gives the appearance that the documentation requirement is an additional requirement as it is not in either extant QC-10, *A Firm's System of Quality Control* or extant AU-C 220, *Quality Control for an Engagement under GAAS*.

The requirement in the first sentence of paragraph 30 is similar to the overall documentation requirement for financial statement audits in AU-C 230, *Audit Documentation* paragraph .08 which states:

The auditor should prepare audit documentation that is sufficient to enable an experienced auditor, having no previous connection with the audit, to understand

- a. the nature, timing, and extent of the audit procedures performed to comply with GAAS and applicable legal and regulatory requirements;
- b. the results of the audit procedures performed, and the audit evidence obtained; and
- c. significant findings or issues arising during the audit, the conclusions reached thereon, and significant professional judgments made in reaching those conclusions

Extant QC-10 paragraph .45 states the firm should establish policies and procedures on documentation of the engagement quality control review, which require documentation that

- a. the procedures required by the firm's policies on engagement quality control review have been performed;
- b. the engagement quality control review has been completed before the report is released; and
- c. the reviewer is not aware of any unresolved matters that would cause the reviewer to believe that the significant judgments that the engagement team made and the conclusions it reached were not appropriate.

Extant AU-C 220 paragraph .26 states that the engagement quality control reviewer should document, for the audit engagement reviewed

- a. that the procedures required by the firm's policies on engagement quality control review have been performed;
- b. the date that the engagement quality control review was completed; and
- c. that the reviewer is not aware of any unresolved matters that would cause the reviewer to believe that the significant judgments that the engagement team made and the conclusions it reached were not appropriate.

The GAO stated the following:

We are concerned that the documentation requirements in the first sentence of Paragraph 30— relating to being sufficient to enable an understanding of the nature, timing, and extent of the procedures performed in the EQR—are not sufficiently clear and may result in an inconsistent level of detail in the documentation of the EQR. The requirement may be over interpreted to require documentation beyond the intent of the standard. Alternatively, it might be interpreted to require only a general discussion of the EQR process. It is likely that documentation in government audit organizations, will be more detailed than may be intended or required. It is also unclear what this requirement incorporates that is not included in the specific requirements in Paragraph 30 a-e, which we believe are appropriate.

This issue was provided to the Task Force. The TF was in support of retaining convergence with ISQM 2 with the recommendation for QM implementation guidance to address the documentation requirements, in collaboration with the GAO.

Question for the ASB:

Should the first sentence in paragraph 30 be deleted?

2. Editorial Review

Agenda items 2A-2C have been through Editorial review and reflect revisions suggested by Editorial and accepted by staff.

Agenda Items Presented:

- **2A** Proposed SQMS *A Firm's System of Quality Control*, marked from January meeting
- **2B** Proposed SQMS *Engagement Quality Reviews*, marked from January meeting
- **2C** Proposed SAS *Quality Management for an Engagement Conducted in Accordance with Generally Accepted Auditing Standards*, marked from January meeting
- **2D** Proposed amendments to GAAS resulting from the QM standards
- **2E** Substantive differences between the IAASB and the ASB QM standards
- **2F** Proposed SQMS *A Firm's System of Quality Control*, marked against ISQM 1
- **2G** Proposed SQMS *Engagement Quality Reviews*, marked against ISQM 2
- **2H** Proposed SAS *Quality Management for an Engagement Conducted in Accordance with Generally Accepted Auditing Standards*, marked against ISA 220 (Revised)
- **2I** Draft "Crosswalk"
- **2J** Executive Summary

Ms. Lord and Mr. Heath will be using agenda items 2A, 2B, 2C, and 2D in the discussion of the proposed standards. Agenda items 2E-2H are presented for information only.

Statement on Quality Management Standards No. 1, *A Firm's System of Quality Management*

Commented [AG1]: Note: For ease of reading and to speed the turnaround and issuance of the final standard, the word "proposed" has been added as a watermark, deleted in the text and not shown in track changes; and references have been updated to refer to SQMS No. 2 and SAS No. 146.

Introduction

Scope of This Statement on Quality Management Standards

1. This Statement on Quality Management Standards (SQMS) deals with a firm's responsibilities to design, implement, and operate a system of quality management for its accounting and auditing practice.
2. Engagement quality reviews form part of the firm's system of quality management and
 - a. this SQMS addresses the firm's responsibility to establish policies or procedures addressing engagements that are required to be subject to engagement quality reviews.
 - b. SQMS No. 2, *Engagement Quality Reviews*, deals with the appointment and eligibility of the engagement quality reviewer, and the performance and documentation of the engagement quality review.
3. Other professional standards include requirements for engagement partners and other engagement team members regarding quality management at the engagement level. For example, Statement on Auditing Standards (SAS) No. 146, *Quality Management for an Engagement Conducted in Accordance With Generally Accepted Auditing Standards*,[‡] deals with the specific responsibilities of the auditor regarding quality management at the engagement level for an audit of financial statements and the related responsibilities of the engagement partner. Other professional standards, including AT-C section 105, *Concepts Common to All Attestation Engagements*,[‡] and AR-C section 60, *General Principles for Engagements Performed in Accordance With Statements on Standards for Accounting and Review Services*,[†] also establish requirements for the engagement partner for the management of quality at the engagement level.
4. This SQMS is to be read in conjunction with the AICPA Code of Professional Conduct (AICPA code) and other relevant ethical requirements. Law, regulation, or relevant ethical

[‡] All AT-C sections can be found in AICPA *Professional Standards*.

[†] All AR-C sections can be found in AICPA *Professional Standards*.

requirements may establish responsibilities for the firm's management of quality beyond those described in this SQMS. (Ref: par. [A2A1](#))

5. This SQMS applies to audit and attestation engagements performed by a firm in accordance with *Government Auditing Standards*. This SQMS does not apply to government audit organizations. Instead, those government audit organizations are subject to the quality control and assurance requirements of *Government Auditing Standards*.
6. This SQMS applies to all firms that perform any engagement included in a firm's accounting and auditing practice. The system of quality management that is established in accordance with the requirements of this SQMS enables the consistent performance by the firm of all such engagements.

The Firm's System of Quality Management

7. A system of quality management operates in a continual and iterative manner and is responsive to changes in the nature and circumstances of the firm and its engagements. It ~~also~~ does not operate in a linear manner. However, for the purposes of this SQMS, a system of quality management addresses the following eight components: (Ref: par. [A3A2](#))
 - a. The firm's risk assessment process
 - b. Governance and leadership
 - c. Relevant ethical requirements
 - d. Acceptance and continuance of client relationships and specific engagements
 - e. Engagement performance
 - f. Resources
 - g. Information and communication
 - h. The monitoring and remediation process
8. This SQMS requires the firm to apply a risk-based approach in designing, implementing, and operating the components of the system of quality management in an interconnected and coordinated manner such that the firm proactively manages the quality of engagements performed by the firm. (Ref: par. [A4A3](#))
9. The risk-based approach is embedded in the requirements of this SQMS through the following:
 - a. *Establishing quality objectives*. The quality objectives established by the firm consist of objectives in relation to the components of the system of quality management that are to be achieved by the firm. The firm is required to establish the quality objectives specified by this SQMS and any additional quality objectives considered necessary by the firm to achieve the objectives of the system of quality management.
 - b. *Identifying and assessing risks to the achievement of the quality objectives* (referred to in this SQMS as *quality risks*). The firm is required to identify and assess quality risks to provide a basis for the design and implementation of responses.

c. Designing and implementing responses to address the quality risks. The nature, timing, and extent of the firm's responses to address the quality risks are based on, and responsive to, the reasons for the assessments given to the quality risks.

10. This SQMS requires that, at least annually, the individual or individuals assigned ultimate responsibility and accountability for the system of quality management, on behalf of the firm, evaluate the system of quality management and conclude whether the system of quality management provides the firm with reasonable assurance that the objectives of the system, stated in paragraph 15a–b, are being achieved. (Ref: par. [A5A4](#))

Scalability

11. In applying a risk-based approach, the firm is required to take into account
- the nature and circumstances of the firm, and
 - the nature and circumstances of the engagements performed by the firm.

Accordingly, the design of the firm's system of quality management, in particular, the complexity and formality of the system, will vary. For example, a firm that performs different types of engagements for a wide variety of entities, such as audits of specialized industries or group audits for multinational entities, will likely need to have a more complex and formalized system of quality management and supporting documentation than a firm that performs only reviews of financial statements or compilation engagements.

Networks and Service Providers

12. This SQMS addresses the firm's responsibilities when the firm
- belongs to a network, and the firm complies with network requirements or uses network services in the system of quality management or in performing engagements, or
 - uses resources from a service provider in the system of quality management or in performing engagements.

Even when the firm complies with network requirements or uses network services or resources from a service provider, the firm is responsible for its system of quality management.

Authority of This Standard

13. Paragraph 15 contains the objective of the firm in following this SQMS. This SQMS contains the following: (Ref: par. [A6A5](#))
- Requirements designed to enable the firm to meet the objective in paragraph 15 (Ref: par. [A7A6](#))
 - Related guidance in the form of application and other explanatory material (Ref: par. [A8A7](#))
 - Introductory material that provides context relevant to a proper understanding of this SQMS

d. Definitions (Ref: par. ~~A9A8~~)

Effective Date

14. Systems of quality management in compliance with this SQMS are required to be designed and implemented by December 15, 2025, and the evaluation of the system of quality management required by paragraphs 54–55 is required to be performed within one year following December 15, 2025.

Objective

15. The objective of the firm is to design, implement, and operate a system of quality management for engagements performed by the firm in its accounting and auditing practice that provides the firm with reasonable assurance that
- a. the firm and its personnel fulfill their responsibilities in accordance with professional standards and applicable legal and regulatory requirements and conduct engagements in accordance with such standards and requirements, and
 - b. engagement reports issued by the firm are appropriate in the circumstances.
16. The public interest is served by the consistent performance of quality engagements. The design, implementation, and operation of the system of quality management enables the consistent performance of quality engagements by providing the firm with reasonable assurance that the objectives of the system of quality management, stated in paragraph 15a–b, are achieved. Quality engagements are achieved through planning and performing engagements and reporting on them in accordance with professional standards and applicable legal and regulatory requirements. Achieving the objectives of those standards and complying with the requirements of applicable law or regulation involves exercising professional judgment and, when applicable to the type of engagement, maintaining professional skepticism.

Definitions

17. For purposes of the SQMSs, the following terms have the meanings attributed as follows:

Accounting and auditing practice. A practice that performs engagements covered by this SQMS, which are audit, attestation, review, compilation, and any other services for which standards have been promulgated by the AICPA Auditing Standards Board (ASB) or the AICPA Accounting and Review Services Committee (~~ARSC~~) under the “General Standards Rule” (ET sec. 1.300.001)[†] or the “Compliance With Standards Rule” (ET sec. 1.310.001) of the AICPA code. (Ref: par. ~~A9A~~A9)

Commented [AG2]: Used in subsequent definition

Deficiency in the firm’s system of quality management (referred to as *deficiency in this SQMS*). This exists when (Ref: par. A10 and ~~A169–A170~~A174–A175)

- a quality objective required to achieve the objective of the system of quality management is not established;

[†] All ET sections can be found in AICPA *Professional Standards*.

- a quality risk, or combination of quality risks, is not identified or properly assessed; (Ref: par. A11)
- a response, or combination of responses, does not reduce to an acceptably low level the likelihood of a related quality risk occurring because the responses are not properly designed, implemented, or operating effectively; or
- another aspect of the system of quality management is absent, or not properly designed, implemented, or operating effectively, such that a requirement of this SQMS has not been addressed. (Ref: par. A12–A13)

Engagement documentation. The record of work performed, results obtained, and conclusions the practitioner reached (terms such as *working papers* or *work papers* are sometimes used).

Engagement partner. The partner or other individual appointed by the firm who is responsible for the engagement and its performance, and for the report that is issued on behalf of the firm, and who, wherewhen required, has the appropriate authority from a professional, legal, or regulatory body.

Commented [AG3]: Editorial

Engagement quality review. An objective evaluation of the significant judgments made by the engagement team and the conclusions reached thereon performed by the engagement quality reviewer and completed on or before the date of the engagement report.

Engagement quality reviewer. A partner, other individual in the firm, or an external individual; appointed by the firm to perform the engagement quality review.

Engagement team. All partners and staff performing the engagement, and any other individuals who perform procedures on the engagement, excluding an external specialist¹ and internal auditors who provide direct assistance on an engagement. (Ref: par. A14)

External inspections. Inspections or investigations, undertaken by an external oversight authority, related to the firm's system of quality management or engagements performed by the firm. (Ref: par. A15)

Findings (in relation to a system of quality management). Information about the design, implementation, and operation of the system of quality management that has been accumulated from the performance of monitoring activities, external inspections, and other relevant sources, which indicates that one or more deficiencies may exist. (Ref: par. A16–A18)

Firm. A form of organization permitted by law or regulation whose characteristics conform to resolutions of the Council of the AICPA and that is engaged in public practice. (Ref: par. A19)

¹ Paragraph .06 of AU-C section 620, *Using the Work of an Auditor's Specialist*, defines the term *auditor's specialist*.

Inspection. Inspection is an evaluation of the adequacy of aspects of the firm’s quality management policies and procedures, its personnel’s understanding of those policies and procedures, and the extent of the firm’s compliance with them.

Network. ~~As defined in “Definitions” (ET sec. 0.400) in the AICPA code, an~~ association of entities that includes one or more firms ~~as defined in “Definitions” in the AICPA code (ET section 0.400).~~ (Ref: par. A20)

Network firm. ~~As defined in “Definitions” (ET sec. 0.400) in the AICPA, a~~ firm or other entity that belongs to a network, ~~as defined in “Definitions” in the AICPA Code of Professional Conduct (ET section 0.400).~~ References to a *network firm* are to be read hereafter as “another firm or entity that belongs to the same network as the firm.”

Commented [AG4]: To be more clear

Partner. Any individual with authority to bind the firm with respect to the performance of a professional services engagement. For purposes of this definition, *partner* may include an employee with this authority who has not assumed the risks and benefits of ownership. Firms might use different titles to refer to individuals with this authority.

Personnel. Partners and staff in the firm. (Ref: par. A21–A22)

Professional judgment. The application of relevant training, knowledge, and experience, within the context of professional standards, in making informed decisions about the courses of action that are appropriate in the design, implementation, and operation of the firm’s system of quality management.

Professional standards. Standards promulgated by the ASB or ~~the AICPA Accounting and Review Services Committee ARSC~~ under the “General Standards Rule” (ET sec. 1.300.001) or the “Compliance With Standards Rule” (ET sec. 1.310.001) of the AICPA code, or other standard-setting bodies that set auditing and attest standards applicable to the engagement being performed and relevant ethical requirements.

Quality objectives. The desired outcomes in relation to the components of the system of quality management to be achieved by the firm.

Quality risk. A risk that has a reasonable possibility of

- occurring, and
- individually, or in combination with other risks, adversely affecting the achievement of one or more quality objectives.

Reasonable assurance. In the context of the SQMSs, a high, but not absolute, level of assurance.

Relevant ethical requirements. Principles of professional ethics and ethical requirements to which the firm, engagement team, engagement quality reviewer, and other firm personnel are subject when undertaking engagements in the firm’s accounting and auditing practice, ~~which that~~ consist of the AICPA ~~Code of Professional Conduct~~ code together with rules of applicable state boards of accountancy and applicable regulatory agencies that are more restrictive. (Ref: par. A23–A24 and A64)

Response (in relation to a system of quality management). Policies or procedures designed and implemented by the firm to address one or more quality risks such as the following: (Ref: par. A25–A27 and A52)

- *Policies* are statements of what should, or should not, be done to address quality risks. Such statements may be documented, explicitly stated in communications, or implied through actions and decisions.
- *Procedures* are actions to implement policies.

Service provider (in the context of this SQMS). An individual or organization external to the firm that provides a resource that is used in the system of quality management or in performing engagements. Service providers exclude the firm’s network, other network firms, or other structures or organizations in the network. (Ref: par. A28 and A110)

Staff. Professionals, other than partners, including any specialists the firm employs.

System of quality management. A system designed, implemented, and operated by a firm to provide the firm with reasonable assurance that

- a. the firm and its personnel fulfill their responsibilities in accordance with professional standards and applicable legal and regulatory requirements, and conduct engagements in accordance with such standards and requirements; and
- b. engagement reports issued by the firm or engagement partners are appropriate in the circumstances.

Commented [AG5]: To be consistent with the objective and extant standard

Requirements

Applying and Complying With Relevant Requirements

18. The firm should comply with each requirement of this SQMS unless the requirement is not relevant to the firm because of the nature and circumstances of the firm or its engagements. (Ref: par. A29)
19. The individual or individuals assigned ultimate responsibility and accountability for the firm’s system of quality management, and the individual or individuals assigned operational responsibility for the firm’s system of quality management, should have an understanding of this SQMS, including the application and other explanatory material, to understand the objective of this SQMS and to apply its requirements properly.

Commented [ACR6]: We have already used the word “understanding” which shortened would basically be saying individuals should have an understanding to understand the objective”

Suggest: should have an understanding of the objective of this SQMS and other explanatory material to be able to apply its requirements properly.

System of Quality Management

20. The firm should design, implement, and operate a system of quality management. In doing so, the firm should exercise professional judgment, taking into account the nature and circumstances of the firm and its engagements. The governance and leadership component of the system of quality management establishes the environment that supports the design, implementation, and operation of the system of quality management (Ref: par. A30–A31)

Commented [AG7R6]: Your suggestion changes the meaning, because the explanatory material is part of the SQMS. I always thought the sentence should say “... should read this SQMS, including the application and OEM, to understand ...and apply...” But that would create a difference with AU-C 200...”

Responsibilities

21. The firm should assign (Ref: par. A32–A36)
 - a. ultimate responsibility and accountability for the system of quality management to the firm’s CEO or the firm’s managing partner (or equivalent) or, if appropriate, the firm’s managing board of partners (or equivalent);
 - b. operational responsibility for the system of quality management; and
 - c. operational responsibility for specific aspects of the system of quality management, including
 - i. compliance with independence requirements, and (Ref: par. A37)
 - ii. the monitoring and remediation process.
22. In assigning the roles in paragraph 21, the firm should determine that the individual or individuals (Ref: par. A38)
 - a. have the appropriate experience, knowledge, influence, and authority within the firm and sufficient time to fulfill their assigned responsibility, and (Ref: par. A39)
 - b. understand their assigned roles and that they are accountable for fulfilling them.
23. The firm should determine that the individual or individuals assigned operational responsibility for the system of quality management, compliance with independence requirements, and the monitoring and remediation process, have a direct line of communication to the individual or individuals assigned ultimate responsibility and accountability for the system of quality management.

The Firm’s Risk Assessment Process

24. The firm should design and implement a risk assessment process to establish quality objectives, identify and assess quality risks, and design and implement responses to address the quality risks. (Ref: par. A40–A42)
25. The firm should establish the quality objectives specified by this SQMS and any additional quality objectives considered necessary by the firm to achieve the objectives of the system of quality management. (Ref: par. A43–A45)
26. The firm should identify and assess quality risks to provide a basis for the design and implementation of responses. In doing so, the firm should do the following:
 - a. Obtain an understanding of the conditions, events, circumstances, actions, or inactions that may adversely affect the achievement of the quality objectives, including the following: (Ref: par. A46–A48)
 - i. With respect to the nature and circumstances of the firm, those relating to
 - (1) the complexity and operating characteristics of the firm;
 - (2) the strategic and operational decisions and actions, business processes, and business model of the firm;

- (3) the characteristics and management style of leadership;
 - (4) the resources of the firm, including the resources provided by service providers;
 - (5) law, regulation, professional standards, and the environment in which the firm operates; and
 - (6) in the case of a firm that belongs to a network, the nature and extent of the network requirements and network services, if any
- ii. With respect to the nature and circumstances of the engagements performed by the firm, those relating to
 - (1) the types of engagements performed by the firm and the reports to be issued, and
 - (2) the types of entities for which such engagements are undertaken
- b. Take into account how, and the degree to which, the conditions, events, circumstances, actions, or inactions in paragraph 26a may adversely affect the achievement of the quality objectives. (Ref: par. A49–A50)
27. The firm should design and implement responses to address the quality risks in a manner that is based on, and responsive to, the reasons for the assessments given to the quality risks. The firm’s responses should ~~also~~ include the responses specified in paragraph 35. However, the responses specified in paragraph 35 alone are not sufficient to achieve the objectives of the system of quality management. (Ref: par. A51–A53)
28. The firm should establish policies or procedures ~~that are~~ designed to identify information ~~indicating that indicates~~ additional quality objectives, or additional or modified quality risks or responses, are needed due to changes in the nature and circumstances of the firm or its engagements. If such information is identified, the firm should consider the information and, when appropriate, (Ref: par. A54–A55)
- a. establish additional quality objectives or modify additional quality objectives previously established by the firm; (Ref: par. A56)
 - b. identify and assess additional quality risks, modify the quality risks, or reassess the quality risks; or
 - c. design and implement additional responses or modify the responses.

Commented [AG8]: Tracy suggested deleting

Commented [AG9]: Editorial

Governance and Leadership

29. The firm should establish the following quality objectives that address the firm’s governance and leadership, which establishes the environment that supports the system of quality management:
- a. The firm demonstrates a commitment to quality through a culture that exists throughout the firm, which recognizes and reinforces the following: (Ref: par. A57–A58)
 - i. The firm’s role in serving the public interest by consistently performing quality engagements

- ii. The importance of professional ethics, values, and attitudes
 - iii. The responsibility of all personnel for quality relating to the performance of engagements or activities within the system of quality management and their expected behavior
 - iv. The importance of quality in the firm's strategic decisions and actions, including the firm's financial and operational priorities
- b. Leadership is responsible and accountable for quality. (Ref: par. A59)
 - c. Leadership demonstrates a commitment to quality through its actions and behaviors. (Ref: par. A60)
 - d. The organizational structure and assignment of roles, responsibilities, and authority is appropriate to enable the design, implementation, and operation of the firm's system of quality management. (Ref: par. A32–A35 and A61)
 - e. Resource needs, including financial resources, are planned for, and resources are obtained, allocated, or assigned in a manner that is consistent with the firm's commitment to quality. (Ref: par. A62–A63)

Relevant Ethical Requirements

30. The firm should establish the following quality objectives that address the fulfillment of responsibilities in accordance with relevant ethical requirements, including those related to independence: (Ref: par. A64–A66 and A68)
- a. The firm and its personnel
 - i. understand the relevant ethical requirements to which the firm and the firm's engagements are subject, and (Ref: par. A23)
 - ii. fulfill their responsibilities in relation to the relevant ethical requirements to which the firm and the firm's engagements are subject.
 - b. Others, including the network, network firms, individuals in the network or network firms, or service providers, who are subject to the relevant ethical requirements to which the firm and the firm's engagements are subject
 - i. understand the relevant ethical requirements that apply to them, and (Ref: par. A23, A67)
 - ii. fulfill their responsibilities in relation to the relevant ethical requirements that apply to them. (Ref: par. A68)

Acceptance and Continuance of Client Relationships and Specific Engagements

31. The firm should establish the following quality objectives that address the acceptance and continuance of client relationships and specific engagements:
- a. Judgments by the firm about whether to accept or continue a client relationship or specific engagement are appropriate based on the following:

- i. Information obtained about the nature and circumstances of the engagement and the integrity and ethical values of the client (including management; and, when appropriate, those charged with governance) that is sufficient to support such judgments (Ref: par. A69–A74)
 - ii. The firm’s ability to perform the engagement in accordance with professional standards and applicable legal and regulatory requirements (Ref: par. A75–A76)
- b. The financial and operational priorities of the firm do not lead to inappropriate judgments about whether to accept or continue a client relationship or specific engagement. (Ref: par. A77–A78)

Engagement Performance

32. The firm should establish the following quality objectives that address the performance of quality engagements:
- a. Engagement teams understand and fulfill their responsibilities in connection with the engagements, including, as applicable, the overall responsibility of engagement partners for managing and achieving quality on the engagement and being sufficiently and appropriately involved throughout the engagement. (Ref: par. A79)
 - b. The nature, timing, and extent of direction and supervision of engagement teams and review of the work performed is appropriate based on the nature and circumstances of the engagements and the resources assigned or made available to the engagement teams; the work performed by less experienced engagement team members is directed, supervised, and reviewed by suitably experienced engagement team members. (Ref: par. A80–A81)
 - c. Engagement teams exercise appropriate professional judgment and, when applicable to the type of engagement, maintain professional skepticism. (Ref: par. A82)
 - d. Consultation on difficult or contentious matters is undertaken, and the conclusions agreed to are implemented. (Ref: par. A83–A85)
 - e. Differences of opinion within the engagement team, or between the engagement team and the engagement quality reviewer or individuals performing activities within the firm’s system of quality management, are brought to the attention of the firm and resolved. (Ref: par. A86)
 - f. Engagement documentation is assembled on a timely basis after the date of the engagement report and is appropriately maintained and retained to meet the needs of the firm and comply with law, regulation, relevant ethical requirements, and professional standards. (Ref: par. A87–A89)

Resources

33. The firm should establish the following quality objectives that address appropriately obtaining, developing, using, maintaining, allocating, and assigning resources in a timely

manner to enable the design, implementation, and operation of the system of quality management: (Ref: par. A90–A91)

Human Resources

- a. Personnel are hired, developed, and retained and have the competence and capabilities to (Ref: par. A92–A94)
 - i. consistently perform quality engagements, including having knowledge or experience relevant to the engagements the firm performs, or
 - ii. perform activities or carry out responsibilities in relation to the operation of the firm’s system of quality management.
- b. Personnel demonstrate a commitment to quality through their actions and behaviors, develop and maintain the appropriate competence to perform their roles, and are held accountable or recognized through timely evaluations, compensation, promotion, and other incentives. (Ref: par. A95–A97)
- c. Individuals are obtained from external sources (that is, the network, another network firm, or a service provider) when the firm does not have sufficient or appropriate personnel to enable the operation of firm’s system of quality management or performance of engagements. (Ref: par. A98)
- d. Engagement team members ~~are assigned to each engagement~~, including an engagement partner, who have appropriate competence and capabilities, including being given sufficient time, to consistently perform quality engagements, ~~are assigned to each engagement~~. (Ref: par. A92–A93, A99–A101)
- e. Individuals who have appropriate competence and capabilities, including sufficient time, to perform such activities are assigned to perform activities within the system of quality management.

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Technological Resources

- f. Appropriate technological resources are obtained or developed, implemented, maintained, and used to enable the operation of the firm’s system of quality management and the performance of engagements. (Ref: par. A102–A106 and A109)

Intellectual Resources

- g. Appropriate intellectual resources are obtained or developed, implemented, maintained, and used to enable the operation of the firm’s system of quality management and the consistent performance of quality engagements, and such intellectual resources are consistent with professional standards and applicable legal and regulatory requirements, where applicable. (Ref: par. A107–A109)

Service Providers

- h. Human, technological, or intellectual resources from service providers are appropriate for use in the firm’s system of quality management and in performing engagements, taking into account the quality objectives in paragraph 33d–g. (Ref: par. A110–A115)

Information and Communication

34. The firm should establish the following quality objectives that address obtaining, generating, or using information regarding the system of quality management and communicating information within the firm and to external parties on a timely basis to enable the design, implementation, and operation of the system of quality management: (Ref: par. A116)
- a. The information system identifies, captures, processes, and maintains relevant and reliable information that supports the system of quality management, whether from internal or external sources. (Ref: par. A117–A119)
 - b. The culture of the firm recognizes and reinforces the responsibility of personnel to exchange information with the firm and with one another. (Ref: par. A120)
 - c. Relevant and reliable information is exchanged throughout the firm and with engagement teams, including the following: (Ref: par. A120)
 - i. Information is communicated to personnel and engagement teams, and the nature, timing, and extent of the information is sufficient to enable them to understand and carry out their responsibilities relating to performing activities within the system of quality management or engagements.
 - ii. Personnel and engagement teams communicate information to the firm when performing activities within the system of quality management or engagements.
 - d. Relevant and reliable information is communicated to external parties, including the following:
 - i. Information is communicated by the firm to or within the firm's network or to service providers, if any, enabling the network or service providers to fulfill their responsibilities relating to the network requirements or network services or resources provided by them. (Ref: par. A121)
 - ii. Information is communicated externally when required by law, regulation, or professional standards or to support external parties' understanding of the system of quality management. (Ref: par. A122–A123)

Specified Responses

35. In designing and implementing responses in accordance with paragraph 27, the firm should include the following responses: (Ref: par. A124)
- a. The firm establishes policies or procedures for
 - i. identifying, evaluating, and addressing threats to compliance with the relevant ethical requirements. (Ref: par. A125)
 - ii. identifying, communicating, evaluating, and reporting of any breaches of the relevant ethical requirements and appropriately responding to the causes and consequences of the breaches in a timely manner. (Ref: par. A126–A127)
 - b. The firm obtains, at least annually, a documented confirmation of compliance with independence requirements from all personnel required by relevant ethical requirements to be independent.

- c. The firm establishes policies or procedures for receiving, investigating, and resolving complaints and allegations about failures to perform work in accordance with professional standards and applicable legal and regulatory requirements or noncompliance with the firm’s policies or procedures established in accordance with this SQMS. (Ref: par. A128–A129)
- d. The firm establishes policies or procedures that address the following circumstances:
 - i. The firm becomes aware of information subsequent to accepting or continuing a client relationship or specific engagement that would have caused it to decline the client relationship or specific engagement had that information been known prior to accepting or continuing the client relationship or specific engagement. (Ref: par. A130–A131)
 - ii. The firm is obligated by law or regulation to accept a client relationship or specific engagement. (Ref: par. A132–A133)
- e. The firm establishes policies or procedures that (Ref: par. A134–A137)
 - i. address when it is appropriate to communicate with external parties about the firm’s system of quality management, and (Ref: par. A138–A140)
 - ii. address the information to be provided when communicating externally about the firm’s system of quality management, including the nature, timing, and extent and appropriate form of communication. (Ref: par. A141–A142)
- f. The firm establishes policies or procedures that address engagement quality reviews in accordance with SQMS No. 2 and requires an engagement quality review for the following:
 - i. Audits or other engagements for which an engagement quality review is required by law or regulation (Ref: par. A143)
 - ii. Audits or other engagements for which the firm determines that an engagement quality review is an appropriate response to address one or more quality risks (Ref: par. A144–A147)

Monitoring and Remediation Process

- 36. The firm should establish a monitoring and remediation process to (Ref: par. A148)
 - a. provide relevant, reliable, and timely information about the design, implementation, and operation of the system of quality management.
 - b. take appropriate actions to respond to identified deficiencies such that deficiencies are remediated on a timely basis.

Designing and Performing Monitoring Activities

- 37. The firm should design and perform monitoring activities to provide a basis for the identification of deficiencies.
- 38. In determining the nature, timing, and extent of the monitoring activities, the firm should take the following into account: (Ref: par. A149–A152)
 - a. The reasons for the assessments given to the quality risks

- b. The design of the responses
 - c. The design of the firm’s risk assessment process and monitoring and remediation process (Ref: par. A153–A155)
 - d. Changes in the system of quality management (Ref: par. A156)
 - e. The results of previous monitoring activities, whether previous monitoring activities continue to be relevant in evaluating the firm’s system of quality management and whether remedial actions to address previously identified deficiencies were effective (Ref: par. A157–A158)
 - f. Other relevant information, including complaints and allegations about failures to perform work in accordance with professional standards and applicable legal and regulatory requirements or noncompliance with the firm’s policies or procedures established in accordance with this SQMS, information from external inspections, and information from service providers (Ref: par. A159–A161)
39. The firm should include the inspection of completed engagements in its monitoring activities and should determine which engagements and engagement partners to select. In doing so, the firm should (Ref: par. A150 and A162–A166)
- a. take into account the matters in paragraph 38;
 - b. consider the nature, timing, and extent of other monitoring activities undertaken by the firm and the engagements and engagement partners subject to such monitoring activities; (Ref: par. A167–~~A168~~) and
 - c. select at least one completed engagement for each engagement partner on a cyclical basis determined by the firm.
40. The firm should establish policies or procedures that
- a. require the individuals performing the monitoring activities to have the competence and capabilities, including sufficient time, to perform the monitoring activities effectively; ~~and~~
 - b. address the objectivity of the individuals performing the monitoring activities, based on the premise that objectivity is enhanced when the engagement team members or the engagement quality reviewer of an engagement ~~is~~are not involved in performing any ~~inspection of monitoring activities related to~~ that engagement. (Ref: par. ~~A168–A169–A173~~)

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Evaluating Findings and Identifying Deficiencies

41. The firm should evaluate findings to determine whether deficiencies exist, including in the monitoring and remediation process. (Ref: par. ~~A170–A174–A178~~)

Evaluating Identified Deficiencies

42. The firm should evaluate the severity and pervasiveness of identified deficiencies by (Ref: par. A173, A175–A176)
- a. investigating the root causes of the identified deficiencies. In determining the nature, timing, and extent of the procedures to investigate the root causes, the firm should

take into account the nature of the identified deficiencies and their possible severity. (Ref: par. A177–A181)

- b. evaluating the effect of the identified deficiencies, individually and in aggregate, on the system of quality management.

Responding to Identified Deficiencies

- 43. The firm should design and implement remedial actions to address identified deficiencies that are responsive to the results of the root cause analysis. (Ref: par. A182–A184)
- 44. The individual or individuals assigned operational responsibility for the monitoring and remediation process should evaluate whether the remedial actions
 - a. are appropriately designed to address the identified deficiencies and their related root causes and determine that they have been implemented.
 - b. implemented to address previously identified deficiencies are effective.
- 45. If the evaluation indicates that the remedial actions are not appropriately designed and implemented or are not effective, the individual or individuals assigned operational responsibility for the monitoring and remediation process should take appropriate action to determine that the remedial actions are appropriately modified such that they are effective.

Findings About a Particular Engagement

- 46. The firm should respond to circumstances ~~when-in which~~ findings indicate that there is an engagement for which required procedures were omitted during the performance of the engagement, or ~~that~~ the report issued may be inappropriate. The firm's response should include the following: (Ref: par. A185)
 - a. Taking appropriate action to comply with relevant professional standards and applicable legal and regulatory requirements
 - b. When the report is considered to be inappropriate, considering the implications and taking appropriate action, including considering whether to obtain legal advice

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Ongoing Communication Related to Monitoring and Remediation

- 47. The individual or individuals assigned operational responsibility for the monitoring and remediation process should communicate the following on a timely basis to the individual or individuals assigned ultimate responsibility and accountability for the system of quality management and the individual or individuals assigned operational responsibility for the system of quality management: (Ref: par. A186)
 - a. A description of the monitoring activities performed
 - b. The identified deficiencies, including the severity and pervasiveness of such deficiencies
 - c. The remedial actions to address the identified deficiencies
- 48. The firm should communicate the matters described in paragraph 47 to engagement teams and other individuals assigned activities within the system of quality management to enable them to take prompt and appropriate action in accordance with their responsibilities.

Network Requirements or Network Services

49. When the firm belongs to a network, the firm should understand the following, when applicable: (Ref: par. A20 and A187–A189)
- The requirements established by the network regarding the firm’s system of quality management, including requirements for the firm to implement or use resources or services designed or otherwise provided by or through the network (that is, network requirements)
 - Any services or resources provided by the network that the firm chooses to implement or use in the design, implementation, or operation of the firm’s system of quality management (that is, network services)
 - The firm’s responsibilities for any actions that are necessary to implement the network requirements or use network services (Ref: par. A190)

The firm remains responsible for its system of quality management, including professional judgments made in the design, implementation, and operation of the system of quality management. The firm should not allow compliance with the network requirements or use of network services to contravene the requirements of this SQMS. (Ref: par. A20 and A191)

50. Based on the understanding obtained in accordance with paragraph 49, the firm should
- determine how the network requirements or network services are relevant to, and are taken into account in, the firm’s system of quality management, including how they are to be implemented. (Ref: par. A192)
 - evaluate whether and, if so, how the network requirements or network services need to be adapted or supplemented by the firm to be appropriate for use in its system of quality management. (Ref: par. A193–A195)

Monitoring Activities Undertaken by the Network on the Firm’s System of Quality Management

51. **In**For circumstances ~~when in which~~ the network performs monitoring activities relating to the firm’s system of quality management, the firm should
- determine the effect of the monitoring activities performed by the network on the nature, timing, and extent of the firm’s monitoring activities performed in accordance with paragraphs 37–39;
 - determine the firm’s responsibilities in relation to the monitoring activities, including any related actions by the firm; and
 - as part of evaluating findings and identifying deficiencies in paragraph 41, obtain the results of the monitoring activities from the network in a timely manner. (Ref: par. A196)

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Monitoring Activities Undertaken by the Network Across the Network Firms

52. The firm should
- understand the overall scope of the monitoring activities undertaken by the network

across the network firms, including monitoring activities to determine that network requirements have been appropriately implemented across the network firms, and how the network will communicate the results of its monitoring activities to the firm.

- b.* at least annually, obtain information from the network about the overall results of the network's monitoring activities across the network firms, if applicable, and (Ref: par. A197–A199)
 - i.* communicate the information to engagement teams and other individuals assigned activities within the system of quality management, as appropriate, to enable them to take prompt and appropriate action in accordance with their responsibilities, and
 - ii.* consider the effect of the information on the firm's system of quality management.

Deficiencies in Network Requirements or Network Services Identified by the Firm

- 53.** If the firm identifies a deficiency in the network requirements or network services, the firm should (Ref: par. A200)
 - a.* communicate to the network relevant information about the identified deficiency, and
 - b.* in accordance with paragraph 43, design and implement remedial actions to address the effect of the identified deficiency in the network requirements or network services. (Ref: par. A201)

Evaluating the System of Quality Management

- 54.** The individual or individuals assigned ultimate responsibility and accountability for the system of quality management should evaluate, on behalf of the firm, the system of quality management. The evaluation should be undertaken as of a point in time and performed at least annually. (Ref: par. A202–A205)
- 55.** Based on the evaluation, the individual or individuals assigned ultimate responsibility and accountability for the system of quality management should conclude, on behalf of the firm, one of the following: (Ref: par. A206 and A213)
 - a.* The system of quality management provides the firm with reasonable assurance that the objectives of the system of quality management are being achieved. (Ref: par. A207)
 - b.* Except for matters related to identified deficiencies that have a severe but not pervasive effect on the design, implementation, and operation of the system of quality management, the system of quality management provides the firm with reasonable assurance that the objectives of the system of quality management are being achieved. (Ref: par. A208)
 - c.* The system of quality management does not provide the firm with reasonable assurance that the objectives of the system of quality management are being achieved. (Ref: par. A208–A212)

56. If the individual or individuals assigned ultimate responsibility and accountability for the system of quality management reaches the conclusion described in paragraph 55*b* or 55*c*, the firm should do the following: (Ref: par. A214)
- a. Take prompt and appropriate action
 - b. Communicate to
 - i. engagement teams and other individuals assigned activities within the system of quality management to the extent that it is relevant to their responsibilities, and (Ref: par. A215)
 - ii. external parties in accordance with the firm’s policies or procedures required by paragraph 35*e*. (Ref: par. A216)
57. The firm should undertake periodic performance evaluations of the individual or individuals assigned ultimate responsibility and accountability for the system of quality management and the individual or individuals assigned operational responsibility for the system of quality management. In doing so, the firm should take into account the evaluation of the system of quality management. (Ref: par. A217–A219)

Documentation

58. The firm should prepare documentation of its system of quality management that is sufficient to (Ref: par. A220–A222)
- a. support a consistent understanding of the system of quality management by personnel, including an understanding of their roles and responsibilities with respect to the system of quality management and performing engagements.
 - b. support the consistent implementation and operation of the responses.
 - c. provide evidence of the design, implementation, and operation of the responses to support the evaluation of the system of quality management by the individual or individuals assigned ultimate responsibility and accountability for the system of quality management.
59. In preparing documentation, the firm should include the following:
- a. Identification of the individual or individuals assigned ultimate responsibility and accountability for the system of quality management and operational responsibility for the system of quality management
 - b. The firm’s quality objectives and quality risks (Ref: par. A223)
 - c. A description of the responses and how the firm’s responses address the quality risks
 - d. Regarding the monitoring and remediation process:
 - i. ~~Evidence~~evidence of the monitoring activities performed;
 - ii. ~~The~~the evaluation of findings, and identified deficiencies and their related root causes; and
 - iii. ~~Remedial~~remedial actions to address identified deficiencies and the evaluation of the design and implementation of such remedial actions.

iv. Communications about monitoring and remediation

- e. The conclusion reached pursuant to paragraph 55 and the basis ~~therefor~~ that conclusion

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60. The firm should document the matters in paragraph 59 as they relate to network requirements or network services and the evaluation of the network requirements or network services in accordance with paragraph 50*b*. (Ref: par. A224)
61. The firm should establish a period of time for the retention of documentation for the system of quality management that is sufficient to enable the firm and its peer reviewer to monitor the design, implementation, and operation of the firm's system of quality management or for a longer period if required by law or regulation.

Application and Other Explanatory Material

Scope of This Standard (Ref: par. 3–4)

~~A1.~~ *[placeholder to retain Exposure Draft numbering]*

~~A2.~~A1. The AICPA code establishes the fundamental principles of professional ethics, which include the obligation to act in a way that serves the public interest.² As indicated in paragraph 16, in the context of engagement performance as described in this SQMS, the consistent performance of quality engagements forms part of the obligation to act in the public interest.

The Firm's System of Quality Management (Ref: par. 7–10)

~~A3.~~A2. The firm may use different terminology or frameworks to describe the components of its system of quality management.

~~A4.~~A3. Examples of the interconnected nature of the components include the following:

- The firm's risk assessment process sets out the process the firm is required to follow in implementing a risk-based approach across the system of quality management.
- The governance and leadership component establishes the environment that supports the system of quality management.
- The resources and information and communication components enable the design, implementation, and operation of the system of quality management.
- The monitoring and remediation process is designed to monitor the entire system of quality management. The results of the monitoring and remediation process provide information that is relevant to the firm's risk assessment process.
- There may be relationships between specific matters; for example, certain aspects of relevant ethical requirements are relevant to accepting and continuing client relationships and specific engagements.

~~A5.~~A4. Reasonable assurance is obtained when the system of quality management reduces to an acceptably low level the risk that the objectives stated in paragraph 15*a–b* are not achieved.

² Paragraph .01 of ET section 0.300.030.

Reasonable assurance is not an absolute level of assurance because there are inherent limitations of a system of quality management. Such limitations include the fact that human judgment in decision making can be faulty and that breakdowns in a firm’s system of quality management may occur, for example, due to human error or behavior or failures in IT applications.

Authority of This Standard (Ref: par. 13)

~~A6:~~A5. The objective of this SQMS provides the context in which the requirements of this SQMS are set, establishes the desired outcome of this SQMS, and is intended to assist the firm in understanding what needs to be accomplished and, when necessary, the appropriate means of doing so.

~~A7:~~A6. The requirements of this SQMS are expressed using the word *should*.

~~A8:~~A7. When necessary, the application and other explanatory material provides further explanation of the requirements and guidance for carrying them out. In particular, it may

- explain more precisely what a requirement means or is intended to cover, and
- include examples that illustrate how the requirements might be applied.

Although such guidance does not, in itself, impose a requirement, it is relevant to the proper application of the requirements. The application and other explanatory material may also provide background information on matters addressed in this SQMS. These additional considerations assist in the application of the requirements in this SQMS. They do not, however, limit or reduce the responsibility of the firm to apply and comply with the requirements in this SQMS.

~~A9:~~A8. This SQMS includes, under the heading, “Definitions,” a description of the meanings attributed to certain terms for purposes of this SQMS. These definitions are provided to assist in the consistent application and interpretation of this SQMS and are not intended to override definitions that may be established for other purposes, whether in law, regulation, or otherwise.

Definitions

Accounting and Auditing Practice (Ref: par. 17)

~~A10:~~A9. ~~A9A.~~ Standards promulgated by the ASB and ~~AICPA Accounting and Review Services Committee~~ARSC that apply to engagements covered by this SQMS comprise the following:

- Statements on Auditing Standards (SASs)
- Statements on Standards for Attestation Engagements (SSAEs)
- Statements on Standards for Accounting and Review Services (SSARSs)

Although standards for other engagements may be promulgated by other AICPA technical committees, engagements performed in accordance with those standards are not encompassed in the definition of an *accounting and auditing practice*.

Deficiency (Ref: par. 17)

A11.A10. The firm identifies deficiencies by evaluating findings. A deficiency may arise from a finding or a combination of findings.

A12.A11. When a deficiency is identified as a result of a quality risk, or combination of quality risks, not being identified or properly assessed, the responses to address such quality risks may also be absent or not appropriately designed or implemented.

A13.A12. The other aspects of the system of quality management consist of the requirements in this SQMS addressing the following:

- Assigning responsibilities (paragraphs 21–22)
- The firm’s risk assessment process
- The monitoring and remediation process
- The evaluation of the system of quality management

A14.A13. Examples of deficiencies related to other aspects of the system of quality management include the following:

- The firm’s risk assessment process fails to identify information that indicates changes in the nature and circumstances of the firm and its engagements and the need to establish additional quality objectives or modify the quality risks or responses.
- The firm’s monitoring and remediation process is not designed or implemented in a manner that
 - provides relevant, reliable, and timely information about the design, implementation, and operation of the system of quality management.
 - enables the firm to take appropriate actions to respond to identified deficiencies such that deficiencies are remediated on a timely basis.
- The individual or individuals assigned ultimate responsibility and accountability for the system of quality management do not undertake the annual evaluation of the system of quality management.

Engagement Team (Ref: par. 17)

A15.A14. SAS No. 146³ provides guidance in applying the definition of *engagement team* in the context of an audit of financial statements. AU-C section 600, *Special Considerations — Audits of Group Financial Statements (Including the Work of Component Auditors)*,⁵⁴ expands on how SAS No. 146 is to be applied in relation to an audit of group financial statements. The quality risks and responses to those risks relevant to group audit engagements may be different for engagement

³ Paragraphs A15–A21 of Statement on Auditing Standards (SAS) No. 146, *Quality Management for an Engagement Conducted in Accordance With Generally Accepted Auditing Standards*.

⁵ All AU-C sections can be found in AICPA *Professional Standards*.

team members who are firm personnel than for engagement team members who are external to the firm (for example, engagement team members who are from network firms or are service providers, such as component auditors from firms not within the firm’s network).

External Inspections (Ref: par. 17)

~~A16:~~A15. In some circumstances, an external oversight authority, such as the U.S. Department of Labor, may undertake other types of inspections, for example, reviews that focus on, for a selection of firms, particular aspects of audit engagements or firm-wide practices.

Findings (Ref: par. 17)

~~A17:~~A16. As part of accumulating findings from monitoring activities, external inspections, and other relevant sources, the firm may identify other observations about the firm’s system of quality management, such as positive outcomes or opportunities for the firm to improve, or further enhance, the system of quality management. Paragraph A168 explains how other observations may be used by the firm in the system of quality management.

~~A18:~~A17. Paragraph A157 provides examples of information from other relevant sources.

~~A19:~~A18. Monitoring activities include monitoring at the engagement level, such as inspection of engagements. Furthermore, external inspections and other relevant sources may include information that relates to specific engagements. As a result, information about the design, implementation, and operation of the system of quality management includes engagement-level findings that may be indicative of findings in relation to the system of quality management.

Firm (Ref: par. 17)

~~A20:~~A19. The definition of *firm* in relevant ethical requirements may differ from the definition set out in this SQMS.

Network (Ref: par. 17 and 49)

~~A21:~~A20. Networks and the firms within the network may be structured in a variety of ways. For example, in the context of a firm’s system of quality management,

- ~~The~~the network may establish requirements for the firm related to its system of quality management or provide services that are used by the firm in its system of quality management or in performing engagements.
- ~~Other~~other firms within the network may provide services (for example, resources) that are used by the firm in its system of quality management or in performing engagements.
- ~~Other~~other structures or organizations within the network may establish requirements for the firm related to its system of quality management or provide services.

For the purposes of this ~~proposed SQMS~~standard, any network requirements or network services that are obtained from the network, another firm within the network, or another structure or organization in the network are considered “network requirements or network services.”

Personnel (Ref: par. 17)

~~A22:~~A21. In addition to personnel (that is, individuals in the firm), the firm may use individuals external to the firm in performing activities in the system of quality management or in

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In this style, it is acceptable for the bullets to stand alone as long as they finish the thought and sentence style of the introductory phrase, so I removed the colon

performing engagements. For example, individuals external to the firm may include individuals from other network firms (for example, individuals in a service delivery center of a network firm) or individuals employed by a service provider (for example, a component auditor from another firm not within the firm’s network).

~~A23.~~A22. Personnel also includes partners and staff in other structures of the firm, such as a service delivery center in the firm.

Relevant Ethical Requirements (Ref: par. 17 and 30)

~~A24.~~A23. The relevant ethical requirements that are applicable in the context of a system of quality management may vary, depending on the nature and circumstances of the firm and its engagements. The AICPA code acknowledges that federal, state, or local statutes, rules, or regulations may be more restrictive than the AICPA code.

~~A25.~~A24. Various provisions of the relevant ethical requirements may apply only to individuals in the context of the performance of engagements and not the firm itself. For example, the “**Integrity and Objectivity Rule**” of the AICPA code (~~ET sec. 1.100.001~~) prohibits individuals from knowingly misrepresenting facts or subordinating their judgment when performing professional services for a client or for an employer (~~ET sec. 1.100.001~~). Compliance with such relevant ethical requirements by individuals may need to be addressed by the firm’s system of quality management.

Response (Ref: par. 17)

~~A26.~~A25. Policies are implemented through the actions of personnel and other individuals whose actions are subject to the policies (including engagement teams) or through their restraint from taking actions that would conflict with the firm’s policies.

~~A27.~~A26. Procedures may be mandated, through formal documentation or other communications, or may result from behaviors that are not mandated but, rather, are conditioned by the firm’s culture. Procedures may be enforced through the actions permitted by IT applications or other aspects of the firm’s IT environment.

~~A28.~~A27. If the firm uses individuals external to the firm in the system of quality management or in performing engagements, different policies or procedures may need to be designed by the firm to address the actions of the individuals. SAS No. 146 ⁵ provides guidance when different policies or procedures may need to be designed by the firm to address the actions of individuals external to the firm in the context of an audit of financial statements.

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Service Provider (Ref: par. 17)

~~A29.~~A28. Service providers include component auditors from other firms not within the firm’s network.

Applying, and Complying With, Relevant Requirements (Ref: par. 18)

~~A30.~~A29. Examples of when a requirement of this SQMS may not be relevant to the firm include the following:

⁵ Paragraphs A23–A25 of SAS No. 146.

- The firm is a sole practitioner. For example, the requirements addressing the organizational structure and assigning roles, responsibilities, and authority within the firm; direction, supervision, and review; and addressing differences of opinion may not be relevant.
- The firm only performs engagements that are preparation of financial statements engagements in accordance with AR-C section 70, *Preparation of Financial Statements*. For example, because the firm is not required to maintain independence for preparation of financial statements engagements, the requirement to obtain a documented confirmation of compliance with independence requirements from all personnel would not be relevant.

System of Quality Management

Design, Implement, and Operate a System of Quality Management (Ref: par. 20)

A31:A30. Quality management is not a separate function of the firm; it is the integration of a culture that demonstrates a commitment to quality with the firm's strategy, operational activities, and business processes. As a result, designing the system of quality management and the firm's operational activities and business processes in an integrated manner may promote a harmonious approach to managing the firm and enhance the effectiveness of quality management.

A32:A31. The quality of professional judgments exercised by the firm is likely to be enhanced when individuals making such judgments demonstrate an attitude that includes an inquiring mind, which involves

- considering the source, relevance, and sufficiency of information obtained about the system of quality management, including information related to the nature and circumstances of the firm and its engagements, and
- being open and alert to a need for further investigation or other action.

Responsibilities (Ref: par. 21–22 and 29d)

A33:A32. The governance and leadership component includes a quality objective that the firm has an organizational structure and assignment of roles, responsibilities, and authority that is appropriate to enable the design, implementation, and operation of the firm's system of quality management.

A34:A33. Notwithstanding the assignment of responsibilities related to the system of quality management in accordance with paragraph 21, the firm remains ultimately responsible for the system of quality management and holding individuals responsible and accountable for their assigned roles. For example, in accordance with paragraphs 54 and 55, although the firm assigns the evaluation of the system of quality management and conclusion thereon to the individual or individuals assigned ultimate responsibility and accountability for the system of quality management, the firm is responsible for the evaluation and conclusion.

A35:A34. Individuals who have the appropriate influence and authority within the firm, as required by paragraph 22, to be assigned responsibility for the matters in paragraph 21 are typically partners of the firm ~~so that they have appropriate influence and authority within the firm, as required~~

~~by paragraph 22.~~ However, based on the legal structure of the firm, there may be circumstances ~~when in which~~ an individual may not be a partner of the firm, but the individual has the appropriate influence and authority within the firm to perform the assigned role because of formal arrangements made by the firm or the firm's network.

Commented [AG17]: Revised for clarity.

~~A36.~~A35. How the firm assigns roles, responsibilities, and authority within the firm may vary, and law or regulation may impose certain requirements for the firm that affect the leadership and management structure or their assigned responsibilities. An individual assigned responsibility for a matter in paragraph 21 may further assign roles, procedures, tasks, or actions to other individuals to assist the individual in fulfilling the responsibilities. However, an individual assigned responsibility for a matter in paragraph 22 remains responsible and accountable for the responsibilities assigned to the individual.

~~A37.~~A36. An example of scalability to demonstrate how assigning roles and responsibilities may be undertaken in firms of different complexity is as follows:

- In a less complex firm, ultimate responsibility and accountability for the system of quality management may be assigned to a single managing partner with sole responsibility for the oversight of the firm. This individual may also assume responsibility for all aspects of the system of quality management, including operational responsibility for the system of quality management, compliance with independence requirements, and the monitoring and remediation process.
- In a more complex firm, the organizational structure of the firm may include the multiple levels of leadership, and the firm may have an independent governing body that has nonexecutive oversight of the firm, which may comprise external individuals. Furthermore, the firm may assign operational responsibility for specific aspects of the system of quality management beyond those specified in paragraph 21c, such as operational responsibility for compliance with ethical requirements or operational responsibility for managing a service line.

~~A38.~~A37. Compliance with independence requirements is essential to the performance of engagements in a firm's accounting and auditing practice and is an expectation of stakeholders relying on the firm's reports. The individual or individuals assigned operational responsibility for compliance with independence requirements are ordinarily responsible for the oversight of all matters related to independence so that a robust and consistent approach is designed and implemented by the firm to deal with independence requirements.

~~A39.~~A38. Law, regulation, or professional standards may establish additional requirements for an individual assigned responsibility for a matter in paragraph 21, such as requirements for professional licensing, professional education, or continuing professional development.

~~A40.~~A39. The appropriate experience and knowledge for the individual or individuals assigned operational responsibility for the system of quality management ordinarily includes an understanding of the firm's strategic decisions and actions and experience with the firm's business operations.

The Firm's Risk Assessment Process (Ref: par. 24)

~~A41.~~A40. How the firm designs the firm's risk assessment process may be affected by the nature and circumstances of the firm, including how the firm is structured and organized.

Examples of scalability to demonstrate how the firm’s risk assessment process may differ from that of other firms include the following:

- In a less complex firm, the individual or individuals assigned operational responsibility for the system of quality management may have a sufficient understanding of the firm and its engagements to undertake the risk assessment process. Furthermore, the documentation of the quality objectives, quality risks, and responses may be less extensive than for a more complex firm (for example, it may be documented in a single document).
- In a more complex firm, there may be a formal risk assessment process involving multiple individuals and numerous activities. The process may be centralized (for example, the quality objectives, quality risks, and responses are established centrally for all business units, functions, and service lines) or decentralized (for example, the quality objectives, quality risks, and responses are established at a business unit, function, or service line level, with the outputs combined at the firm level). The firm’s network may also provide the firm with quality objectives, quality risks, and responses to be included in the firm’s system of quality management.

A42:A41. The process of establishing quality objectives, identifying and assessing quality risks, and designing and implementing responses is iterative, and the requirements of this SQMS are not intended to be addressed in a linear manner. Examples of the iterative and nonlinear nature of the firm’s risk assessment process include the following:

- In identifying and assessing quality risks, the firm might determine that an additional quality objective needs to be established.
- When designing and implementing responses, the firm might determine that a quality risk was not identified and assessed.

A43:A42. Information sources that enable the firm to establish quality objectives, identify and assess quality risks, and design and implement responses are part of the firm’s information and communication component and include the following:

- The results of the firm’s monitoring and remediation process (see paragraphs 43 and A169).
- Information from the network or service providers, including
 - information about network requirements or network services (see paragraph 49), and
 - other information from the network, including information about the results of monitoring activities undertaken by the network across the network firms (see paragraphs 51–52).

Other information, whether internal or external, may also be relevant to the firm’s risk assessment process, such as the following:

- Information regarding complaints and allegations about failures to perform work in accordance with professional standards and applicable legal and regulatory requirements or noncompliance with the firm’s policies or procedures established in accordance with this SQMS

- The results of external inspections
- Information from regulators about the entities for whom the firm performs engagements, ~~which that~~ is made available to the firm, such as information from a securities regulator about an entity for whom the firm performs engagements (for example, irregularities in the entity’s financial statements or noncompliance with securities regulations)
- Changes in the system of quality management that affect other aspects of the system; for example, changes in the firm’s resources
- Other external sources, such as regulatory actions and litigation against the firm or other firms in the jurisdiction that may highlight areas for the firm to consider

Establish Quality Objectives (Ref: par. 25)

~~A44.~~A43. Law, regulation, or professional standards may establish requirements that give rise to additional quality objectives. For example, if a firm is required by law or regulation to appoint nonexecutive individuals to the firm’s governance structure, the firm may consider it necessary to establish additional quality objectives to address the requirements.

~~A45.~~A44. While the nature and circumstances of the firm and its engagements are specific to the firm, the quality objectives are sufficiently comprehensive such that it is unlikely that the firm would find it necessary to establish additional quality objectives.

~~A46.~~A45. The firm may establish sub-objectives to enhance the firm’s identification and assessment of quality risks, and design and implementation of responses.

Identify and Assess Quality Risks (Ref: par. 26)

~~A47.~~A46. There may be other conditions, events, circumstances, actions, or inactions not described in paragraph 26a that may adversely affect the achievement of a quality objective.

~~A48.~~A47. A risk arises from how, and the degree to which, a condition, event, circumstance, action, or inaction may adversely affect the achievement of a quality objective. Not all risks meet the definition of a *quality risk*. Professional judgment assists the firm in determining whether a risk is a quality risk, which is based on the firm’s consideration of whether there is a reasonable possibility of the risk occurring; and, individually; or in combination with other risks, adversely affecting the achievement of one or more quality objectives.

~~A49.~~A48. Examples of the firm’s understanding of the conditions, events, circumstances, actions, or inactions that may adversely affect the achievement of the quality objectives and the related quality risks are as follows:

<p>Examples of the firm’s understanding of the conditions, events, circumstances, actions, or inactions that may adversely affect the achievement of the quality objectives</p>	<p>Examples of quality risks that may arise</p>
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<p>The strategic and operational decisions and actions, business processes, and business model of the firm: The firm’s overall financial goals are overly dependent on the extent of services provided by the firm not within the scope of this SQMS.</p>	<p>In the context of governance and leadership, this may give rise to a number of quality risks such as the following:</p> <ul style="list-style-type: none"> • Resources are allocated or assigned in a manner that prioritizes the services not within the scope of this SQMS and may negatively affect the quality of engagements within the scope of this SQMS. • Decisions about financial and operational priorities do not fully or adequately consider the importance of quality in performing engagements within the scope of this SQMS.
<p>The characteristics and management style of leadership: The firm is a smaller firm with a few engagement partners with shared authority.</p>	<p>In the context of governance and leadership, this may give rise to a number of quality risks such as the following:</p> <ul style="list-style-type: none"> • Leadership’s responsibilities and accountability for quality are not clearly defined and assigned. • The actions and behaviors of leadership that do not promote quality are not questioned.
<p>The complexity and operating characteristics of the firm: The firm has recently completed a merger with another firm.</p>	<p>In the context of resources, this may give rise to a number of quality risks, including the following:</p> <ul style="list-style-type: none"> • Technological resources used by the two merged firms may be incompatible. • Engagement teams may use intellectual resources developed by a firm prior to the merger, which are no

longer consistent with the new methodology being used by the new merged firm.

A50:A49. Given the evolving nature of the system of quality management, the responses designed and implemented by the firm may give rise to conditions, events, circumstances, actions, or inactions that result in further quality risks. For example, the firm may implement a resource (for example, a technological resource) to address a quality risk, and quality risks may arise from the use of such resource.

A51:A50. The degree to which a risk, individually or in combination with other risks, may adversely affect the achievement of a quality objective may vary based on the conditions, events, circumstances, actions, or inactions giving rise to the risk, taking matters such as the following into account:

- How the condition, event, circumstance, action, or inaction would affect the achievement of the quality objective
- How frequently the condition, event, circumstance, action, or inaction is expected to occur
- How long it would take after the condition, event, circumstance, action, or inaction occurred for it to have an effect, and whether in that time the firm would have an opportunity to respond to mitigate the effect of the condition, event, circumstance, action, or inaction-
- How long the condition, event, circumstance, action, or inaction would affect the achievement of the quality objective once it has occurred-

The assessment of quality risks need not comprise formal ratings or scores, although firms are not precluded from using them.

Design and Implement Responses to Address the Quality Risks (Ref: par. 17 and 27)

A52:A51. The nature, timing, and extent of the responses are based on the reasons for the assessment given to the quality risks, ~~which is the firm's consideration of whether there is a reasonable possibility of the risk occurring, and individually, or in combination with other risks, adversely affecting the achievement of one or more quality objectives.~~

A53:A52. The responses designed and implemented by the firm may operate at the firm level or engagement level, or there may be a combination of responsibilities for actions to be taken at the firm and engagement level. An example of a response designed and implemented by the firm that operates at both the firm and engagement level is as follows:

The firm establishes policies or procedures for consultation, which include with whom consultation should be undertaken by engagement teams and the specific matters for which consultation is required. The firm appoints suitably qualified and experienced individuals to provide the consultations. The engagement team is responsible for identifying when matters

Commented [AG18]: As directed by the ASB in January

for consultation occur ~~and~~, initiating consultation, and implementing the conclusions from consultation.⁶

Commented [AG19]: Added this footnote but had to manually number

~~A54:A53.~~ The need for formally documented policies or procedures may be greater for firms that have many personnel or that are geographically dispersed, in order to achieve consistency across the firm.

Changes in the Nature and Circumstances of the Firm or Its Engagements (Ref: par. 28)

~~A55:A54.~~ Examples of scalability to demonstrate how policies or procedures for identifying information about changes in the nature and circumstances of the firm and its engagements may vary from other firms include the following:

- In a less complex firm, the firm may have informal policies or procedures to identify information about changes in the nature and circumstances of the firm or its engagements, particularly when the individual or individuals responsible for establishing quality objectives, identifying and assessing quality risks, and designing and implementing responses are able to identify such information in the normal course of their activities.
- In a more complex firm, the firm may need to establish more formal policies or procedures to identify and consider information about changes in the nature and circumstances of the firm or its engagements. This may include, for example, a periodic review of information relating to the nature and circumstances of the firm and its engagements, including ongoing tracking of trends and occurrences in the firm's internal and external environment.

~~A56:A55.~~ Additional quality objectives may need to be established, or quality risks and responses added to or modified, as part of the remedial actions undertaken by the firm to address an identified deficiency in accordance with paragraph 43.

~~A57:A56.~~ The firm may have established quality objectives in addition to those specified by this SQMS. The firm may also identify information that indicates that additional quality objectives previously established by the firm are no longer needed or need to be modified.

Governance and Leadership

Commitment to Quality (Ref: par. 29a)

~~A58:A57.~~ The firm's culture is an important factor in influencing the behavior of personnel. Relevant ethical requirements ordinarily establish the principles of professional ethics and are further addressed in the "Relevant Ethical Requirements" section of this SQMS. Professional values and attitudes may include the following:

- Professional manner~~s~~; for example, timeliness, courteousness, respect, accountability, responsiveness, and dependability
- A commitment to teamwork
- Maintaining an open mind to new ideas or different perspectives in the professional environment

⁶ Paragraph 35 of SAS No. 146.

- Pursuit of excellence
- A commitment to continual improvement (for example, setting expectations beyond the minimum requirements and placing a focus on continual learning)
- Social responsibility

~~A59.~~A58. The firm's strategic decision-making process, including the establishment of a business strategy, may include matters such as the firm's decisions about financial and operational matters, the firm's financial goals, how financial resources are managed, growth of the firm's market share, industry specialization, or new service offerings. The firm's financial and operational priorities may directly or indirectly affect the firm's commitment to quality, for example, the firm may have incentives ~~that are~~ focused on financial and operational priorities that may discourage behaviors that demonstrate a commitment to quality.

Leadership (Ref: par. 29b and 29c)

~~A60.~~A59. The responses designed and implemented by the firm to hold leadership responsible and accountable for quality include the performance evaluations required by paragraph 57.

~~A61.~~A60. Although leadership establishes the tone at the top through its actions and behaviors, clear, consistent, and frequent actions and communications at all levels within the firm collectively contribute to the firm's culture and ~~demonstrates~~demonstrate a commitment to quality.

Organizational Structure (Ref: par. 29d)

~~A62.~~A61. The organizational structure of the firm may include operating units, operational processes, divisions, or geographical locations and other structures. In some instances, the firm may concentrate or centralize processes or activities in a service delivery center, and engagement teams may include personnel from the firm's service delivery center who perform specific tasks that are repetitive or specialized in nature.

Resources (Ref: par. 29e)

~~A63.~~A62. The individual or individuals assigned ultimate responsibility and accountability or operational responsibility for the system of quality management are, in most cases, able to influence the nature and extent of resources that the firm obtains, develops, uses, and maintains and how those resources are allocated or assigned, including the timing of when they are used.

~~A64.~~A63. Because resource needs may change over time, it may not be practicable to anticipate all resource needs. The firm's resource planning may involve determining the resources currently required, forecasting the firm's future resource needs, and establishing processes to deal with unanticipated resource needs when they arise.

Relevant Ethical Requirements (Ref: par. 17 and 30)

~~A65.~~A64. The AICPA code sets out the fundamental principles of ethics that provide the framework for the rules that govern the performance of professional responsibilities. The fundamental principles are responsibilities, the public interest, integrity, objectivity and independence, due care, and scope and nature of services. Independence requirements are set forth in the "Independence Rule" (ET sec. 1.200.001) and related interpretations of the AICPA code and

the rules of state boards of accountancy and applicable regulatory agencies. Guidance on threats to independence and safeguards to mitigate such threats involving matters that are not explicitly addressed in the AICPA code are set forth in the “Conceptual Framework for Independence” (ET sec. 1.210.010).

A66:A65. In some cases, the matters addressed by the firm in its system of quality management may be more specific than, or additional to, the provisions of relevant ethical requirements. Examples of matters that a firm may include in its system of quality management that are more specific than, or additional to, the provisions of relevant ethical requirements include the following:

- The firm prohibits the acceptance of gifts and hospitality from a client, even if the value is trivial and inconsequential.
- The firm sets rotation periods for all engagement partners, including those performing attestation, review, and compilation engagements.

A67:A66. Other components may affect or relate to the relevant ethical requirements component. Examples of relationships between the relevant ethical requirements component and other components include the following:

- The information and communication component may address the communication of various matters related to relevant ethical requirements, including
 - the firm communicating the independence requirements to all personnel and others subject to independence requirements.
 - personnel and engagement teams communicating relevant information to the firm without fear of reprisals, such as situations that may create threats to independence or breaches of relevant ethical requirements.
- As part of the resources component, the firm may
 - assign individuals to manage and monitor compliance with relevant ethical requirements or to provide consultation on matters related to relevant ethical requirements.
 - use IT applications to monitor compliance with relevant ethical requirements, including recording and maintaining information about independence.

A68:A67. The relevant ethical requirements that apply to others depend on the provisions of the relevant ethical requirements and how the firm uses others in its system of quality management or in performing engagements. Examples of relevant ethical requirements that apply to others include the following:

- Relevant ethical requirements may include requirements for independence that apply to network firms or employees of network firms; for example, the AICPA code includes independence requirements that apply to network firms.
- Relevant ethical requirements may include a definition of *engagement team* or other similar concept, and the definition may include any individual who performs assurance procedures on the engagement (for example, a service provider engaged to attend a physical inventory count at a remote location). Accordingly, any requirements of the

relevant ethical requirements that apply to the engagement team as defined in the relevant ethical requirements, or other similar concept, may also be relevant to such individuals.

- The principle of confidentiality may apply to the firm’s network, other network firms, or service providers when they have access to client information obtained by the firm.

~~A69:A68.~~ AU-C section 600⁶ states that when the component auditor is ~~not~~ subject to the AICPA code, compliance with the ethics and independence requirements set forth in the ~~International Federation of Ethics Standards Board for~~ Accountants *Code of Ethics for Professional Accountants* ~~is sufficient to fulfill the component auditor’s ethical responsibilities in the group audit.~~⁷ The firm may use, for example, confirmations, letters of representation, or other affirmations from network firms, employees of network firms, or service providers regarding the fulfillment of ethical requirements that are relevant to the firm.

Commented [ACR20]: This is different from the entity mentioned in the footnote, so making sure that this all looks good.

Commented [AG21R20]: Nice catch!

Acceptance and Continuance of Client Relationships and Specific Engagements

The Nature and Circumstances of the Engagement and the Integrity and Ethical Values of the Client (Ref: par. 31a(i))

~~A70:A69.~~ The information obtained about the nature and circumstances of the engagement may include the following:

- The industry of the entity for which the engagement is being undertaken and relevant regulatory factors
- The nature of the entity; ~~for example, its operations, organizational structure, ownership and governance, its business model, and how it is financed~~
- The nature of the underlying subject matter and the applicable criteria; ~~for example, in the case of sustainability reporting:~~
 - ~~The~~the underlying subject matter may include social, environmental, or health and safety information.
 - ~~The~~the applicable criteria may be performance measures established by a recognized body of specialists.

~~A71:A70.~~ The information obtained to support the firm’s judgments about the integrity and ethical values of the client may include the identity and business reputation of the client’s principal owners, key management, and those charged with its governance.

~~A72:A71.~~ Examples of factors that may affect the nature and extent of information obtained about the integrity and ethical values of the client include the following:

⁶ Paragraph .A46 of AU-C section 600, *Special Considerations — Audits of Group Financial Statements (Including the Work of Component Auditors)*.

⁷ The section, “Application of the AICPA Code” (ET sec. 0.200.020), of the AICPA Code of Professional Conduct (AICPA code) explains that an AICPA member who is the group engagement partner will not be considered in violation of the AICPA code if a component auditor practicing outside the United States departs from the AICPA code with respect to the audit or review of group financial statements, as long as the component auditor’s conduct, at a minimum, is in accordance with the ethics and independence requirements set forth in the International Ethics Standards Board for Accountants’ Code of Ethics for Professional Accountants.

- The nature of the entity for which the engagement is being performed, including the complexity of its ownership and management structure
- The nature of the client's operations, including its business practices
- Information concerning the attitude of the client's principal owners, key management, and those charged with its governance ~~towards~~toward such matters as aggressive interpretation of accounting standards and the internal control environment
- Whether the client is aggressively concerned with keeping the firm's fees as low as possible
- Indications of a client-imposed limitation in the scope of work
- Indications that the client might be involved in money laundering or other criminal activities
- The reasons for the proposed appointment of the firm and non-reappointment of the previous firm
- The identity and business reputation of related parties

A73:A72. The firm may obtain the information from a variety of internal and external sources, including the following:

- In the case of an existing client, information from current or previous engagements, if applicable, or inquiry of other personnel who have performed other engagements for the client.
- In the case of a new client, inquiry of existing or previous providers of auditing services to the client, in accordance with relevant ethical requirements.
- Discussions with other third parties, such as bankers, legal counsel, and industry peers.
- Background searches of relevant databases (which may be intellectual resources). In some cases, the firm may use a service provider to perform the background search.

A74:A73. Information that is obtained during the firm's acceptance and continuance process also may often be relevant to the engagement team when planning and performing the engagement. Professional standards may specifically require the engagement team to obtain or consider such information. For example, SAS No. 146⁸ requires the engagement partner to take into account information obtained in the acceptance and continuance process in planning and performing the audit engagement.

A75:A74. Professional standards or applicable legal and regulatory requirements may include specific provisions that need to be addressed before accepting or continuing a client relationship or specific engagement and may also require the firm to make inquiries of an existing or predecessor firm when accepting an engagement. For example, when there has been a change of auditors, AU-C section 210, *Terms of Engagement*,⁹ requires the auditor, prior to starting an initial audit, to request management to authorize the predecessor auditor to respond fully to the auditor's inquiries regarding matters that will assist the auditor in determining whether to accept the

⁸ Paragraph 23 of SAS No. 146.

⁹ Paragraph .11 of AU-C section 210, *Terms of Engagement*.

engagement. ~~The~~The “Conflicts of Interest for Members in Public Practice” interpretation of the AICPA code also addresses consideration of conflicts of ~~interests~~interest in accepting or continuing a client relationship or specific engagement (ET sec. 1.110.010).

The Firm’s Ability to Perform Engagements (Ref: par. 31a(ii))

~~A76:~~A75. The firm’s ability to perform the engagement in accordance with professional standards and applicable legal and regulatory requirements may be affected by the following:

- The availability of appropriate resources to perform the engagement
- Having access to information to perform the engagement or to the persons who provide such information
- Whether the firm and the engagement team are able to fulfill their responsibilities in relation to the relevant ethical requirements

~~A77:~~A76. Examples of factors the firm may consider in determining whether appropriate resources are available to perform the engagement include the following:

- The circumstances of the engagement and the reporting deadline.
- The availability of individuals with the appropriate competence and capabilities, including sufficient time, to perform the engagement. This includes having
 - individuals to take overall responsibility for directing and supervising the engagement,
 - individuals with knowledge of the relevant industry or the underlying subject matter or criteria to be applied in the preparation of the subject matter information and experience with relevant regulatory or reporting requirements, and
 - individuals to perform audit procedures on the financial information of a component for purposes of an audit of group financial statements.
- The availability of specialists, if needed.
- If an engagement quality review is needed, whether there is an individual available who meets the eligibility requirements in SQMS No. 2.
- The need for technological resources; for example, IT applications that enable the engagement team to perform procedures on the entity’s data.
- The need for intellectual resources; for example, a methodology, industry or subject-matter-specific guides, or access to information sources.

The Firm’s Financial and Operational Priorities (Ref: par. 31b)

~~A78:~~A77. Financial priorities may focus on the profitability of the firm, and fees obtained for performing engagements have an effect on the firm’s financial resources. Operational priorities may include strategic focus areas, such as growth of the firm’s market share, industry specialization, or new service offerings. There may be circumstances ~~when~~in which the firm is satisfied with the fee quoted for an engagement, but it is not appropriate for the firm to accept or continue the engagement or client relationship (for example, when the client lacks integrity and ethical values).

~~A79.~~A78. There may be other circumstances ~~when~~in which the fee quoted for an engagement is not sufficient given the nature and circumstances of the engagement, and it may diminish the firm's ability to perform the engagement in accordance with professional standards and applicable legal and regulatory requirements. ~~The~~The "Fees and Other Types of Remuneration" rule of the AICPA code addresses fees and other types of remuneration (ET section ~~0.300.030.041.500~~).

Commented [ACR22]: I added the name of the principle mentioned, but it doesn't look like it discusses fees and remuneration, so I was wondering if the number is wrong.

Engagement Performance

Responsibilities of the Engagement Team and Direction, Supervision, and Review (Ref: par. 32a and 32b)

~~A80.~~A79. Professional standards or applicable legal and regulatory requirements may include specific provisions regarding the overall responsibility of the engagement partner. For example, SAS No. 146 deals with the overall responsibility of the engagement partner for managing and achieving quality on the engagement and for being sufficiently and appropriately involved throughout the engagement, including taking responsibility for appropriate direction and supervision of the engagement team and review of ~~their~~its work.

Commented [ACR23]: Need a verb here, perhaps, such as "taking" or "being responsible for the appropriate direction..."

~~A81.~~A80. Examples of direction, supervision, and review include the following:

- Direction and supervision of the engagement team may include
 - tracking the progress of the engagement,
 - considering the following with respect to members of the engagement team:
 - Whether they understand their instructions
 - Whether the work is being carried out in accordance with the planned approach to the engagement
 - addressing matters arising during the engagement, considering their significance, and modifying the planned approach appropriately, and
 - identifying matters for consultation or consideration by more experienced engagement team members during the engagement.
- A review of work performed may include considering whether
 - the work has been performed in accordance with the firm's policies or procedures, professional standards, and applicable legal and regulatory requirements;
 - significant matters have been raised for further consideration;
 - appropriate consultations have been undertaken, and the resulting conclusions have been documented and implemented;
 - there is a need to revise the nature, timing, and extent of planned work;
 - the work performed supports the conclusions reached and is appropriately documented;
 - the evidence obtained for an assurance engagement is sufficient and appropriate to support the report; and
 - the objectives of the engagement procedures have been achieved.

~~A82.~~~~A81.~~ In some circumstances, the firm may use personnel from a service delivery center in the firm or individuals from a service delivery center in another network firm to perform procedures on the engagement; (that is, the personnel or other individuals are included in the engagement team). In such circumstances, the firm's policies or procedures may specifically address the direction and supervision of the individuals and review of their work, such as

- what aspects of the engagement may be assigned to individuals in the service delivery center;
- how the engagement partner, or their designee, is expected to direct, supervise, and review the work undertaken by individuals in the service delivery center; and
- the protocols for communication between the engagement team and individuals in the service delivery center.

Professional Judgment and Professional Skepticism (Ref: par. 32c)

~~A83.~~~~A82.~~ Professional skepticism supports the quality of judgments made on an assurance engagement and, through these judgments, the overall effectiveness of the engagement team in performing the assurance engagement. Other professional standards may address the exercise of professional judgment or maintenance of professional skepticism at the engagement level. For example, SAS No. 146¹⁰ provides examples of impediments to the maintenance of professional skepticism at the engagement level, unconscious auditor biases that may impede the maintenance of professional skepticism, and possible actions that the engagement team may take to mitigate such impediments.

Consultation (Ref: par. 32d)

~~A84.~~~~A83.~~ Consultation typically involves a discussion at the appropriate professional level, with individuals within or outside the firm who have specialized expertise; on difficult or contentious matters. An environment that reinforces the importance and benefit of consultation and encourages engagement teams to consult may contribute to supporting a culture that demonstrates a commitment to quality.

~~A85.~~~~A84.~~ Difficult or contentious matters on which consultation is needed may either be specified by the firm, or the engagement team may identify matters that require consultation. The firm may also specify how conclusions should be agreed upon and implemented.

~~A86.~~~~A85.~~ SAS No. 146¹¹ includes requirements for the engagement partner related to consultation.

Differences of Opinion (Ref: par. 32e)

~~A87.~~~~A86.~~ The firm may encourage identifying differences of opinion at an early stage and may specify the steps to be taken in raising and dealing with them, including how the matter is to be resolved and how the related conclusions should be implemented and documented. In some circumstances, resolving differences of opinion may be achieved through consulting with another practitioner or firm, or a professional or regulatory body.

¹⁰ Paragraphs A34–A36 of SAS No. 146.

¹¹ Paragraph 35 of SAS No. 146.

Engagement Documentation (Ref: par. 32f)

~~A88.~~A87. Law, regulation, or professional standards may prescribe the time limits by which the assembly of final engagement files for specific types of engagements are to be completed. When no such time limits are prescribed, the time limit may be determined by the firm. For example, in the case of engagements conducted in accordance with ~~Statements on Standards for Attestation Engagements (the SSAEs)~~ or ~~Statements on Standards for Accounting and Review Services (SSARs)~~, an appropriate time limit within which to complete the assembly of the final engagement file is ordinarily not more than 60 days after the date of the engagement report.

Commented [ACR24]: These have previously been mentioned, so acronyms may be used, if you like

~~A89.~~A88. The retention and maintenance of engagement documentation may include managing the safe custody, integrity, accessibility, or retrievability of the underlying data and the related technology. The retention and maintenance of engagement documentation may involve the use of IT applications. The integrity of engagement documentation may be compromised if it is altered, supplemented, or deleted without authorization to do so, or if it is permanently lost or damaged.

~~A90.~~A89. Law, regulation, or professional standards may prescribe the retention periods for engagement documentation. If the retention periods are not prescribed, the firm may consider the nature of the engagements performed by the firm and the firm's circumstances, including whether the engagement documentation is needed to provide a record of matters of continuing significance to future engagements. In the case of engagements conducted under generally accepted auditing standards or the SSAEs, the retention period is ordinarily no shorter than five years from the date of the engagement report, or, if later, the date of the auditor's report on the group financial statements, when applicable.

Resources (Ref: par. 33)

~~A91.~~A90. Resources for the purposes of the resources component include the following:

- Human resources
- Technological resources; for example, IT applications
- Intellectual resources; for example, written policies or procedures, a methodology, or guides

Financial resources are also relevant to the system of quality management because they are necessary for obtaining, developing, and maintaining the firm's human resources, technological resources, and intellectual resources. Given that the management and allocation of financial resources is strongly influenced by leadership, the quality objectives in governance and leadership, such as those that address financial and operational priorities, address financial resources.

~~A92.~~A91. Resources may be internal to the firm or may be obtained externally from the firm's network, another network firm, or service provider. Resources may be used in performing activities within the firm's system of quality management or in performing engagements as part of operating the system of quality management. In circumstances whenin which a resource is obtained from the firm's network or another network firm, paragraphs 49–53 form part of the responses designed and implemented by the firm in achieving the objectives in this component.

Human Resources

Hiring, Developing, and Retaining Personnel and Personnel Competence and Capabilities (Ref: par. 33a and d)

A93.A92. Competence is the ability of the individual to perform a role and goes beyond knowledge of principles, standards, concepts, facts, and procedures; it is the integration and application of technical competence, professional skills, and professional ethics, values, and attitudes. Competence can be developed through a variety of methods, including professional education, continuing professional development, training, work experience, or coaching of less experienced engagement team members by more experienced engagement team members.

A94.A93. Law, regulation, or professional standards may establish requirements addressing competence and capabilities. For example, law or regulation may establish requirements for the professional licensing of engagement partners, including requirements regarding their professional education and continuing professional development.

A95.A94. The policies or procedures designed and implemented by the firm relating to hiring, developing, and retaining personnel may address, for example, the following:

- Recruiting individuals who have, or are able to develop, appropriate competence
- Training programs focused on developing the competence of personnel and continuing professional development
- Evaluation mechanisms that are undertaken at appropriate intervals and include competency areas and other performance measures
- Compensation, promotion, and other incentives, for all personnel, including engagement partners and individuals assigned roles and responsibilities related to the firm's system of quality management.

Personnel's Commitment to Quality and Accountability and Recognition for Commitment to Quality (Ref: par. 33b)

A96.A95. Timely evaluations and feedback help support and promote the continual development of the competence of personnel. Less formal methods of evaluation and feedback may be used, such as in the case of firms with fewer personnel.

A97.A96. Positive actions or behaviors demonstrated by personnel may be recognized through various means, such as through compensation, promotion, or other incentives. In some circumstances, simple or informal incentives that are not based on monetary rewards may be appropriate.

A98.A97. The manner in which the firm holds personnel accountable for actions or behaviors that negatively affect quality, such as failing to demonstrate a commitment to quality, develop and maintain the competence to perform their role, or implement the firm's responses as designed, may depend on the nature of the action or behavior, including its severity and frequency of occurrence. The following are some actions the firm may take when personnel demonstrate actions or behaviors that negatively affect quality:

- Training or other professional development

- Considering the effect of the matter on the evaluation, compensation, promotion, or other incentives of those involved
- Disciplinary action, if appropriate

Individuals Obtained From External Sources (Ref: par. 33c)

~~A99~~A98. Professional standards may include responsibilities for the engagement partner regarding the appropriateness of resources. For example, SAS No. 146¹² addresses the responsibility of the engagement partner for determining that sufficient and appropriate resources to perform the engagement are assigned or made available to the engagement team in a timely manner in accordance with the firm's policies or procedures.

Engagement Team Members Assigned to Each Engagement (Ref: par. 33d)

~~A100~~A99. Engagement team members may be assigned to engagements by

- the firm, including assigning personnel from a service delivery center in the firm.
- the firm's network or another network firm when the firm uses individuals from the firm's network or another network firm to perform procedures on the engagement (for example, a component auditor or a service delivery center of the network or another network firm).
- a service provider when the firm uses individuals from a service provider to perform procedures on the engagement (for example, a component auditor from a firm not within the firm's network).

~~A101~~A100. SAS No. 146¹³ addresses the responsibility of the engagement partner to determine that members of the engagement team, and any auditor's external specialists and internal auditors who provide direct assistance (who are not part of the engagement team), collectively have the appropriate competence and capabilities, including sufficient time, to perform the engagement. The responses designed and implemented by the firm to address the competence and capabilities of engagement team members assigned to the engagement may include policies or procedures that address the following:

- Information that may be obtained by the engagement partner and factors to consider in determining that the engagement team members assigned to the engagement, including those assigned by the firm's network, another network firm, or service provider, have the competence and capabilities to perform the engagement
- How concerns about the competence and capabilities of engagement team members, in particular, those assigned by the firm's network, another network firm, or service provider, may be resolved

~~A102~~A101. The requirements in paragraphs 49–53 are also applicable when using individuals from the firm's network or another network firm on an engagement, including component auditors (see, for example, paragraph A190).

¹² Paragraph 25 of SAS No. 146.

¹³ Paragraph 26 of SAS No. 146.

Technological Resources (Ref: par. 33f)

A103.A102. Technological resources, which are typically IT applications, form part of the firm's IT environment. The firm's IT environment also includes the supporting IT infrastructure and the IT processes and human resources involved in those processes:

- An IT application is a program or a set of programs that is designed to perform a specific function directly for the user or, in some cases, for another application program.
- The IT infrastructure comprises the IT network, operating systems, and databases and their related hardware and software.
- The IT processes are the firm's processes to manage access to the IT environment, program changes or changes to the IT environment, and IT operations, which includes monitoring the IT environment.

A104.A103. A technological resource may serve multiple purposes within the firm, and some of the purposes may be unrelated to the system of quality management. Technological resources that are relevant for the purposes of this SQMS are as follows:

- Technological resources that are directly used in designing, implementing, or operating the firm's system of quality management
- Technological resources that are used directly by engagement teams in performing engagements
- Technological resources that are essential to enabling the effective operation of the preceding, such as, in relation to an IT application, the IT infrastructure and IT processes supporting the IT application

A105.A104. Examples of scalability to demonstrate how the technological resources that are relevant for the purposes of this SQMS may differ in firms of different complexity include the following:

- In a less complex firm, the technological resources may comprise a commercial IT application used by engagement teams, ~~which that~~ has been purchased from a service provider. The IT processes that support the operation of the IT application may also be relevant, although they may be simple (for example, processes for authorizing access to the IT application and processing updates to the IT application).
- In a more complex firm, the technological resources may be more complex and may comprise the following:
 - Multiple IT applications, including custom-developed applications or applications developed by the firm's network, such as
 - IT applications used by engagement teams (for example, engagement software and automated audit tools) and
 - IT applications developed and used by the firm to manage aspects of the system of quality management (for example, IT applications to monitor independence or assign personnel to engagements)

- The IT processes that support the operation of these IT applications, including the individuals responsible for managing the IT infrastructure and processes and the firm’s processes for managing program changes to IT applications

~~A106-A105.~~ The firm may consider the following matters in obtaining, developing, implementing, and maintaining an IT application:

- The data inputs are complete and appropriate.
- Confidentiality of the data is preserved.
- The IT application operates as designed and achieves the purpose for which it is intended.
- The outputs of the IT application achieve the purpose for which they will be used.
- The general IT controls necessary to support the IT application’s continued operation as designed are appropriate.
- The need for specialized skills to use the IT application effectively, including the training of individuals who will use the IT application.
- The need to develop procedures that set out how the IT application operates.

~~A107-A106.~~ The firm may specifically prohibit the use of IT applications or features of IT applications until such time that it has been determined that they operate appropriately and have been approved for use by the firm. Alternatively, the firm may establish policies or procedures to address circumstances ~~when-in which~~ the engagement team uses an IT application that is not approved by the firm. Such policies or procedures may require the engagement team to determine that the IT application is appropriate for use prior to using it on the engagement, through considering the matters in paragraph A102. SAS No. 146¹⁴ addresses the engagement partner’s responsibilities for engagement resources.

Intellectual Resources (Ref: par. 33g)

~~A108-A107.~~ Intellectual resources include the ~~quality management information and~~ materials the firm uses to enable the operation of the system of quality management and promote consistency in performing engagements. Examples of intellectual resources include written policies or procedures, a methodology, industry or subject-matter-specific guides, accounting guides, standardized documentation, or access to information sources (for example, subscriptions to websites that provide in-depth information about entities or other information that is typically used in performing engagements).

~~A109-A108.~~ Intellectual resources may be made available through technological resources; for example, the firm’s methodology may be embedded in the IT application that facilitates the planning and performance of the engagement.

Commented [AG25]: As agreed by the ASB in January

¹⁴ Paragraphs 25–28 of SAS No. 146.

Use of Technological and Intellectual Resources (Ref: par. 33f–g)

~~A110~~A109. The firm may establish policies or procedures regarding the use of the firm's technological and intellectual resources. Examples of such policies or procedures include the following:

- Requiring the use of certain IT applications or intellectual resources in performing engagements, or relating to other aspects of the engagement, such as in archiving the engagement file
- Specifying the qualifications or experience that individuals need to use the resource, including the need for ~~an~~ specialist or training; for example, the firm may specify the qualifications or expertise needed to use an IT application that analyzes data, given that specialized skills may be needed to interpret the results
- Specifying the responsibilities of the engagement partner regarding the use of technological and intellectual resources
- Setting out how the technological or intellectual resources are to be used, including how individuals should interact with an IT application or how the intellectual resource should be applied, and the availability of support or assistance in using the technological or intellectual resource

Service Providers (Ref: par. 17 and 33h)

~~A111~~A110. In some circumstances, the firm may use resources that are provided by a service provider, particularly in circumstances ~~when~~ in which the firm does not have access to the appropriate resources internally. Notwithstanding that a firm may use resources from a service provider, the firm remains responsible for its system of quality management.

~~A112~~A111. Examples of resources from a service provider include the following:

- Individuals engaged to perform the firm's monitoring activities or engagement quality reviews, or to provide consultation on technical matters
- A commercial IT application used to perform audit engagements
- Individuals performing procedures on the firm's engagements; for example, component auditors from firms not within the firm's network or individuals engaged to attend a physical inventory count at a remote location
- An auditor's external specialist used by the firm to assist the engagement team in obtaining audit evidence

~~A113~~A112. In identifying and assessing quality risks, the firm is required to obtain an understanding of the conditions, events, circumstances, actions, or inactions that may adversely affect the achievement of the quality objectives, which includes conditions, events, circumstances, actions, or inactions relating to service providers. In doing so, the firm may consider the nature of the resources provided by service providers, how and the extent to which they will be used by the firm, and the general characteristics of the service providers used by the firm (for example, the varying types of other professional services firms that are used) to identify and assess quality risks related to the use of such resources.

~~A114~~-~~A113~~. In determining whether a resource from a service provider is appropriate for use in the firm's system of quality management or performing engagements, the firm may obtain information about the service provider and the resource it provides from a number of sources. The following are matters the firm may consider:

- The related quality objective and quality risks. For example, in the case of a methodology from a service provider, there may be quality risks related to the quality objective in paragraph 33g, such as a quality risk that the service provider does not update the methodology to reflect changes in professional standards and applicable legal and regulatory requirements.
- The nature and scope of the resources and the conditions of the service (for example, in relation to an IT application, how often updates will be provided, limitations on the use of the IT application, and how the service provider addresses confidentiality of data).
- The extent to which the resource is used across the firm, how the resource will be used by the firm, and whether it is suitable for that purpose.
- The extent of customization of the resource for the firm.
- The firm's previous use of the service provider.
- The service provider's experience in the industry and reputation in the market.
- The results of ~~assurance~~~~attestation~~ engagements performed by independent third parties on the resource (for example, assurance engagements on quality control materials or reports on service organization controls).

Commented [AG26]: As directed by the ASB in January

~~A115~~-~~A114~~. The firm may have a responsibility to take further actions in using the resource from a service provider so that the resource functions effectively. For example, the firm may need to communicate information to the service provider in order for the resource to function effectively; or, in relation to an IT application, the firm may need to have supporting IT infrastructure and IT processes in place.

~~A116~~-~~A115~~. The evaluation of a service provider from a firm not within the firm's network that is used as a component auditor may be different than that of a service provider engaged directly by the firm. For example, in understanding the competency of the component auditor to perform the engagement, it may not be necessary or practicable for the firm to obtain an understanding of how the component auditor updates its methodology to reflect changes in professional standards. Rather, the firm could perform procedures such as review of results of regulatory inspections, transparency or audit quality information published by the component auditor's firm, or evaluation of the reputation of the component auditor.

Information and Communication (Ref: par. 34)

~~A117~~-~~A116~~. Obtaining, generating, or communicating information is generally an ongoing process that involves all personnel and encompasses the dissemination of information within the firm and externally. Information and communication are pervasive to all components of the system of quality management.

The Firm's Information System (Ref: par. 34a)

~~A118~~A117. Reliable and relevant information includes information that is accurate, complete, timely, and valid to enable the proper functioning of the firm's system of quality management and to support decisions regarding the system of quality management.

~~A119~~A118. The information system may include the use of manual or IT elements, which affect the manner in which information is identified, captured, processed, maintained, and communicated. The procedures to identify, capture, process, maintain, and communicate information may be enforced through IT applications; and in some cases, may be embedded within the firm's responses for other components. In addition, digital records may replace or supplement physical records.

~~A120~~A119. An example of scalability is that less complex firms with fewer personnel and direct involvement of leadership may not need rigorous policies and procedures that specify how information should be identified, captured, processed, and maintained.

Communication Within the Firm (Ref: par. 34b–c)

~~A121~~A120. The firm may recognize and reinforce the responsibility of personnel and engagement teams to exchange information with the firm and one another by establishing communication channels to facilitate communication across the firm. Examples of communication among the firm, engagement teams, and other individuals include the following:

- The firm communicates the responsibility for implementing the firm's responses to personnel and engagement teams.
- The firm communicates changes to the system of quality management to personnel and engagement teams to the extent that the changes are relevant to their responsibilities and enables personnel and engagement teams to take prompt and appropriate action in accordance with their responsibilities.
- The firm communicates information that is obtained during the firm's acceptance and continuance process that is relevant to engagement teams in planning and performing engagements.
- Engagement teams communicate the following information to the firm:
 - Information about the client that is obtained during the performance of an engagement that may have caused the firm to decline the client relationship or specific engagement had that information been known prior to accepting or continuing the client relationship or specific engagement.
 - Information about the operation of the firm's responses (for example, concerns about the firm's processes for assigning personnel to engagements~~s~~) which, in some cases, may indicate a deficiency in the firm's system of quality management.
- Engagement teams communicate information to the engagement quality reviewer or individuals providing consultation.

- Group engagement teams communicate matters to component auditors in accordance with the firm's policies or procedures, including matters related to quality management at the engagement level.
- The individual or individuals assigned operational responsibility for compliance with independence requirements communicate to relevant personnel and engagement teams changes in the independence requirements and the firm's policies or procedures to address such changes.

Communication With External Parties

Communication to or Within the Firm's Network and to Service Providers (Ref: par. 34d(i))

A122-A121. In addition to the firm communicating information to or within the firm's network or to a service provider, the firm may need to obtain information from the network, a network firm, or a service provider that supports the firm in the design, implementation, and operation of its system of quality management. For example, the firm may obtain information from the network or other network firms about clients of other network firms when there are independence requirements that affect the firm.

Communication With Others External to the Firm (Ref: par. 34d(ii))

A123-A122. Examples of when law, regulation, or professional standards may require the firm to communicate information to external parties include the following:

- The firm becomes aware of noncompliance with laws and regulations by a client, and relevant ethical requirements require the firm to report the noncompliance with laws and regulations to an appropriate authority outside the client entity or to consider whether such reporting is an appropriate action in the circumstances.
- Law or regulation requires the firm to publish a transparency report and specifies the nature of the information that is required to be included in the transparency report.
- Securities law or regulation requires the firm to communicate certain matters to those charged with governance.

Paragraphs A131–A135 address communications to support external parties' understanding of the system of quality management beyond those required by law, regulation, or professional standards.

A124-A123. In some cases, law or regulation may preclude the firm from communicating information related to its system of quality management externally. Examples of when the firm may be precluded from communicating information externally include the following:

- Confidentiality law or regulation prohibits disclosure of certain information.
- Law, regulation, or relevant ethical requirements include provisions addressing the duty of confidentiality.

Specified Responses (Ref: par. 35)

~~A125~~~~A124~~. The specified responses may address multiple quality risks related to more than one quality objective across different components. For example, policies or procedures for complaints and allegations may address quality risks related to quality objectives in resources (for example, personnel’s commitment to quality), relevant ethical requirements, and governance and leadership.

Relevant Ethical Requirements (Ref: par. 35a–b)

~~A126~~~~A125~~. Relevant ethical requirements may contain provisions regarding the identification and evaluation of threats and how they should be addressed. For example, the AICPA code provides a conceptual framework for this purpose and, in applying the conceptual framework, requires that the firm use the reasonable and informed third-party test.

~~A127~~~~A126~~. Relevant ethical requirements may specify how the firm is required to respond to a breach. For example, the “Breach of an Independence” interpretation (ET sec. 1.298.010) of the “Independence Rule” (ET sec. 1.200.001) contains guidance addressing a breach of an independence interpretation of the AICPA code, which also contains guidance addressing a breach of any other provision of the AICPA code.

~~A128~~~~A127~~. Matters the firm may address relating to breaches of the relevant ethical requirements include the following:

- The communication of breaches of the relevant ethical requirements to appropriate personnel
- The evaluation of the significance of a breach and its effect on compliance with relevant ethical requirements
- The actions to be taken to satisfactorily address the consequences of a breach, including that such actions be taken as soon as practicable
- Determining whether to report a breach to external parties, such as those charged with governance of the entity to which the breach relates or an external oversight authority
- Determining the appropriate actions to be taken in relation to the individual or individuals responsible for the breach

Complaints and Allegations (Ref: par. 35c)

~~A129~~~~A128~~. Establishing policies or procedures for dealing with complaints and allegations may assist the firm in preventing engagement reports from being issued that are inappropriate. It also may assist the firm in

- identifying and dealing with individuals, including leadership, who do not act or behave in a manner that demonstrates a commitment to quality and supports the firm’s commitment to quality, or
- identifying deficiencies in the system of quality management.

~~A130~~~~A129~~. Complaints and allegations may be made by personnel or others external to the firm (for example, clients, component auditors, or individuals within the firm’s network).

Information That Becomes Known Subsequent to Accepting or Continuing a Client Relationship or Specific Engagement (Ref: par. 35d)

~~A131~~A130. Information that becomes known subsequent to accepting or continuing a client relationship or specific engagement may

- have existed at the time of the firm's decision to accept or continue the client relationship or specific engagement, and the firm was not aware of such information, or
- relate to new information that has arisen since the decision to accept or continue the client relationship or specific engagement.

~~A132~~A131. Examples of matters addressed in the firm's policies or procedures for circumstances in which information becomes known subsequent to accepting or continuing a client relationship or specific engagement that may have affected the firm's decision to accept or continue a client relationship or specific engagement include the following:

- Undertaking consultation within the firm or with legal counsel
- Considering whether there is a professional, legal, or regulatory requirement for the firm to continue the engagement
- Discussing with the appropriate level of the client's management and with those charged with governance or the engaging party the action that the firm might take based on the relevant facts and circumstances
- When it is determined that withdrawal is an appropriate action:
 - Informing the client's management and those charged with governance or the engaging party of this decision and the reasons for the withdrawal
 - Considering whether there is a professional, legal, or regulatory requirement for the firm to report the withdrawal from the engagement, or from both the engagement and the client relationship, together with the reasons for the withdrawal, to regulatory authorities

~~A133~~A132. In some circumstances, law or regulation may impose an obligation on the firm to accept or continue a client engagement.

~~A134~~A133. Examples of matters addressed in the firm's policies or procedures in circumstances in which the firm is obligated to accept or continue an engagement or the firm is unable to withdraw from an engagement, and the firm is aware of information that would have caused the firm to decline or discontinue the engagement, include the following:

- The firm considers the effect of the information on the performance of the engagement.
- The firm communicates the information to the engagement partner and requests the engagement partner to increase the extent and frequency of the direction and supervision of the engagement team members and review of their work.
- The firm assigns more experienced personnel to the engagement.
- The firm determines that an engagement quality review should be performed.

Communication With External Parties (Ref: par: 35e)

A135-A134. The firm’s ability to maintain stakeholder confidence in the quality of its engagements may be enhanced through relevant, reliable, and transparent communication by the firm about the activities that it has undertaken to address quality and the effectiveness of those activities.

A136-A135. External parties who may use information about the firm’s system of quality management, and the extent of their interest in the firm’s system of quality management, may vary based on the nature and circumstances of the firm and its engagements.

A137-A136. Examples of external parties who may use information about the firm’s system of quality management include the following:

- Management or those charged with governance of the firm’s clients may use the information to determine whether to appoint the firm to perform an engagement.
- External oversight authorities may have indicated a desire for the information to support their responsibilities in monitoring the quality of engagements across a jurisdiction and in understanding the work of firms.
- Other firms who use the work of the firm in performing engagements (for example, in relation to a group audit) may have requested such information.
- Other users of the firm’s engagement reports, such as investors who use engagement reports in their decision making, may have indicated a desire for the information.

A138-A137. The information about the system of quality management provided to external parties, including information communicated to those charged with governance about how the system of quality management supports the consistent performance of quality engagements, may address such matters as the following:

- The nature and circumstances of the firm, such as the organizational structure, business model, strategy, and operating environment
- The firm’s governance and leadership, ~~such as its culture, how it demonstrates a commitment to quality, and assigned roles, responsibilities, and authority with respect to the system of quality management~~
 - its culture;
 - how it demonstrates a commitment to quality; and
 - how roles, responsibilities, and authority with respect to the system of quality management are assigned
- How the firm fulfills its responsibilities in accordance with relevant ethical requirements, including those related to independence
- Factors that contribute to quality engagements; for example, such information may be presented in the form of engagement quality indicators with narrative to explain the indicators
- The results of the firm’s monitoring activities and external inspections and how the firm has remediated identified deficiencies or is otherwise responding to them

Commented [ACR27]: Unclear as to which of these are separate ideas:

-Its culture
-How it demonstrates a commitment to quality
-Assigned roles, responsibilities, and authority with respect to the system of quality management

If these are the three concepts, the third one needs a little revision and the whole thing probably needs some semi-colons

Commented [AG28R27]: I revised for clarity

- The evaluation undertaken in accordance with paragraphs 54–55 of whether the system of quality management provides the firm with reasonable assurance that the objectives of the system are being achieved and the conclusion thereon, including the basis for the judgments made in evaluating and concluding
- How the firm has responded to emerging developments and changes in the circumstances of the firm or its engagements, including how the system of quality management has been adapted to respond to such changes
- The relationship between the firm and the network, the overall structure of the network, a description of network requirements and network services, the responsibilities of the firm and the network (including that the firm is ultimately responsible for the system of quality management), and information about the overall scope and results of network monitoring activities across the network firms

Determining When It Is Appropriate to Communicate With External Parties (Ref: par. 35e(i))

~~A139~~A138. The firm's determination of when it is appropriate to communicate with external parties about the firm's system of quality management is a matter of professional judgment and may be influenced by matters such as the following:

- The types of engagements performed by the firm
- The types of entities for which such engagements are undertaken; for example, entities that may have public interest or public accountability characteristics, such as
 - entities that hold a significant amount of assets in a fiduciary capacity for a large number of stakeholders, including financial institutions, such as certain banks, insurance companies, and pension funds;
 - entities with a high public profile or whose management or owners have a high public profile; and
 - entities with a large number and wide range of stakeholders.
- The nature and circumstances of the firm
- The nature of the firm's operating environment, such as customary business practice in the firm's jurisdiction and the characteristics of the financial markets in which the firm operates
- The extent to which the firm has already communicated with external parties in accordance with law or regulation (that is, whether further communication is needed; and, if so, the matters to be communicated)
- The expectations of stakeholders in the firm's jurisdiction, including the understanding and interest that external parties have expressed about the engagements undertaken by the firm, and the firm's processes in performing the engagements
- Jurisdictional trends
- The information that is already available to external parties

- How external parties may use the information, and their general understanding of matters related to firms' ~~systems~~~~systems~~ of quality management and engagements performed by the firm in its accounting and auditing practice
- The public interest benefits of external communication and whether it would reasonably be expected to outweigh the costs (monetary or otherwise) of such communication

Commented [ACR29]: Checking to make sure plural possessive is correct here (because then I think it should be "systems")

The preceding matters may also affect the information provided by the firm in the communication and the nature, timing, and extent and appropriate form of communication.

~~A140-A139.~~ AU-C section 260, *The Auditor's Communication With Those Charged With Governance*, deals with the auditor's responsibility to communicate with those charged with governance in an audit of financial statements and addresses the auditor's determination of the appropriate person or persons within the entity's governance structure with whom to communicate¹⁵ and the communication process.¹⁶ In some circumstances, it may be appropriate to include information about the firm's system of quality management in those communications with those charged with governance (or when performing other engagements, for example, review or examination engagements). How the communication with those charged with governance is undertaken (that is, by the firm or the engagement team) may depend on the firm's policies or procedures and the circumstances of the engagement.

Considerations for Engagements for Governmental Organizations

~~A141-A140.~~ The firm may determine it is appropriate to communicate to those charged with governance of a governmental organization about how the firm's system of quality management supports the consistent performance of quality engagements, taking into account the size and complexity of the governmental organization, the range of its stakeholders, the nature of the services it provides, and the roles and responsibilities of those charged with governance.

Nature, Timing, and Extent and Appropriate Form of Communication With External Parties (Ref: par: 35e(ii))

~~A142-A141.~~ The firm may consider the following attributes in preparing information that is communicated to external parties:

- The information is specific to the circumstances of the firm. Relating the matters in the firm's communication directly to the specific circumstances of the firm may help to minimize the potential that such information becomes overly standardized and less useful over time.
- The information is presented in a clear and understandable manner, and the manner of presentation is neither misleading nor would inappropriately influence the users of the communication (for example, the information is presented in a manner that is appropriately balanced towards positive and negative aspects of the matter being communicated).

¹⁵ Paragraphs .07–.09 of AU-C section 260, *The Auditor's Communication With Those Charged With Governance*.

¹⁶ Paragraphs .15–.20 of AU-C section 260.

- The information is accurate and complete in all material respects and does not contain information that is misleading.
- The information takes into consideration the information needs of the users for whom it is intended. In considering the information needs of the users, the firm may consider matters such as the level of detail that users would find meaningful and whether users have access to relevant information through other sources (for example, the firm’s website).

~~A143-A142.~~ The firm uses professional judgment in determining, in the circumstances, the appropriate form of communication with the external party, including communication with those charged with governance when performing an audit of financial statements of listed entities, which may be made orally or in writing. Accordingly, the form of communication may vary.

Examples of forms of communication to external parties include the following:

- A publication such as a transparency report or audit quality report
- Targeted written communication to specific stakeholders (for example, information about the results of the firm’s monitoring and remediation process)
- Direct conversations and interactions with the external party (for example, discussions between the engagement team and those charged with governance)
- A web page
- Other forms of digital media, such as social media, or interviews or presentations via webcast or video

Engagements Subject to an Engagement Quality Review

Engagement Quality Review Required by Law or Regulation (Ref: par. 35f(i))

~~A144-A143.~~ Law or regulation may require an engagement quality review to be performed, for example, for audit engagements for entities that

- are *public interest entities* as defined in a particular jurisdiction,
- are governmental organizations or recipients of government funding, or entities with public accountability,
- operate in certain industries (for example, financial institutions such as banks, insurance companies, and pension funds),
- meet a specified asset threshold, or
- are under the management of a court or judicial process (for example, liquidation).

Engagement Quality Review as a Response to Address One or More Quality Risks (Ref: par. 35f(ii))

~~A145-A144.~~ The firm’s understanding of the conditions, events, circumstances, actions, or inactions that may adversely affect the achievement of the quality objectives as required by paragraph 26a(ii), relates to the nature and circumstances of the engagements performed by the firm. In designing and implementing responses to address one or more quality risks, the firm may

determine that an engagement quality review is an appropriate response based on the reasons for the assessments given to the quality risks.

~~A146~~, A145. Criteria established by the firm to determine whether an engagement quality review is an appropriate response for one or more quality risks may relate to the types of engagements performed by the firm and reports to be issued, and the types of entities for which engagements are undertaken. Examples of conditions, events, circumstances, actions, or inactions giving rise to such quality risks include the following:

Those relating to the types of engagements performed by the firm and reports to be issued:

- Engagements that involve a high level of complexity or judgment, such as the following:
 - Audits of financial statements for entities operating in an industry that typically has accounting estimates with a high degree of estimation uncertainty (for example, certain large financial institutions or mining entities) or for entities for which uncertainties exist related to events or conditions that may cast significant doubt on their ability to continue as a going concern
 - Assurance engagements that require specialized skills and knowledge in measuring or evaluating the underlying subject matter against the applicable criteria (for example, a greenhouse gas statement in which there are significant uncertainties associated with the quantities reported therein)
- Engagements on which issues have been encountered, such as audit engagements with recurring internal or external inspection findings, unremediated significant deficiencies in internal control, or a material restatement of comparative information in the financial statements
- Engagements for which unusual circumstances have been identified during the firm's acceptance and continuance process (for example, a new client that had a disagreement with its previous auditor or assurance practitioner~~;-)~~)
- Engagements that involve reporting on financial or nonfinancial information that is expected to be included in a regulatory filing~~;~~ and that may involve a higher degree of judgment, such as pro forma financial information to be included in a prospectus

Those relating to the types of entities for which engagements are undertaken:

- Entities in emerging industries or for which the firm has no previous experience~~;~~
- Entities for which concerns were expressed in communications from regulators~~;~~
- Entities that may have public interest or public accountability characteristics, ~~for~~ examples such as the following:
 - Entities that hold a significant amount of assets in a fiduciary capacity for a large number of stakeholders, including financial institutions~~;~~ such as certain banks, insurance companies, and pension funds for which an engagement quality review is not otherwise required by law or regulation
 - Entities with a high public profile or whose management or owners have a high public profile

- Entities with a large number and wide range of stakeholders
- Governmental organizations
 - Due to their size and complexity, the range of their stakeholders or the nature of the services they provide
 - Due to the complexity, and importance to users, of additional reporting requirements established by law or regulation (for example, a separate report on instances of noncompliance with law or regulation to the legislature or other governing body or communicating such instances in the auditor's report on the financial statements)

~~A147~~A146. The firm's responses to address quality risks may include other forms of engagement reviews that are not an engagement quality review. For example, for audits of financial statements, the firm's responses may include reviews of the engagement team's procedures relating to significant risks, or reviews of certain significant judgments, by personnel who have specialized technical expertise. In some cases, these other types of engagement reviews may be undertaken in addition to an engagement quality review.

~~A148~~A147. In some cases, the firm may determine that there are no audits or other engagements for which an engagement quality review or another form of engagement review is an appropriate response to address the quality risks.

Monitoring and Remediation Process (Ref: par. 36–48)

~~A149~~A148. In addition to enabling the evaluation of the system of quality management, the monitoring and remediation process facilitates the proactive and continual improvement of engagement quality and the system of quality management. Examples follow:

- Given the inherent limitations of a system of quality management, the firm's identification of deficiencies is not unusual, and it is an important aspect of the system of quality management because prompt identification of deficiencies enables the firm to remediate them in a timely and effective manner and contributes to a culture of continual improvement.
- The monitoring activities may provide information that enables the firm to prevent a deficiency through responding to a finding that could, over a period of time, lead to a deficiency.

Designing and Performing Monitoring Activities (Ref: par. 38–39)

~~A150~~A149. The firm's monitoring activities may comprise a combination of ongoing monitoring activities and periodic monitoring activities. Ongoing monitoring activities are generally routine activities built into the firm's processes and performed on a real-time basis. Periodic monitoring activities are conducted at certain intervals by the firm. In most cases, ongoing monitoring activities provide information about the system of quality management in a timelier manner.

~~A151~~A150. Monitoring activities may include the inspection of in-process engagements. Inspections of engagements are designed to monitor whether an aspect of the system of quality management is designed, implemented, and operating in the manner intended. In some

circumstances, the system of quality management may include responses that are designed to review engagements while they are in the process of being performed that appear similar in nature to an inspection of in-process engagements (for example, reviews that are designed to detect failures or shortcomings in the system of quality management so that they can prevent a quality risk from occurring). The purpose of the activity drives its design and implementation and where it fits within the system of quality management (that is, whether it is an inspection of an in-process engagement that is a monitoring activity or a review of an engagement that is a response to address a quality risk).

~~A152.~~A151. The nature, timing, and extent of the monitoring activities may also be affected by other matters, including

- the size, structure, and organization of the firm~~;~~
- the involvement of the firm's network in monitoring activities~~;~~ and
- the resources that the firm intends to use to enable monitoring activities, such as the use of IT applications.

~~A153.~~A152. When performing monitoring activities, the firm may determine that changes to the nature, timing, and extent of the monitoring activities are needed, such as when findings indicate the need for more extensive monitoring activities.

The Design of the Firm's Risk Assessment Process and Monitoring and Remediation Process
(Ref: par. 38c)

~~A154.~~A153. How the firm's risk assessment process is designed (for example, a centralized or decentralized process, or the frequency of review) may affect the nature, timing, and extent of the monitoring activities, including monitoring activities over the firm's risk assessment process.

~~A155.~~A154. How the firm's monitoring and remediation process is designed (that is, the nature, timing, and extent of the monitoring and remediation activities, taking into account the nature and circumstances of the firm) may affect the monitoring activities undertaken by the firm to determine whether the monitoring and remediation process is achieving the intended purpose as described in paragraph 36.

~~A156.~~A155. An example of scalability to demonstrate how the monitoring activities for the monitoring and remediation process may differ in firms of different complexity is as follows:

- In a less complex firm, the monitoring activities may be simple because information about the monitoring and remediation process may be readily available in the form of leadership's knowledge, based on their frequent interaction with the system of quality management, of the nature, timing, and extent of the monitoring activities undertaken, the results of the monitoring activities, and the firm's actions to address the results.
- In a more complex firm, the monitoring activities for the monitoring and remediation process may be specifically designed to determine that the monitoring and remediation process is providing relevant, reliable, and timely information about the system of quality management, and responding appropriately to identified deficiencies.

Changes in the System of Quality Management (Ref: par. 38d)

~~A157-A156.~~ Changes in the system of quality management may include

- changes to address an identified deficiency in the system of quality management, ~~and~~
- changes to the quality objectives, quality risks, or responses as a result of changes in the nature and circumstances of the firm and its engagements.

When changes occur, previous monitoring activities undertaken by the firm may no longer provide the firm with information to support the evaluation of the system of quality management and, therefore, the firm's monitoring activities may include monitoring of those areas of change.

Previous Monitoring Activities (Ref: par. 38e and 44b)

~~A158-A157.~~ The results of the firm's previous monitoring activities may indicate areas of the system where a deficiency may arise, particularly areas where there is a history of identified deficiencies.

~~A159-A158.~~ Previous monitoring activities undertaken by the firm may no longer provide the firm with information to support the evaluation of the system, including on areas of the system of quality management that have not changed, particularly when time has elapsed since the monitoring activities were undertaken.

Other Relevant Information (Ref: par. 17 and 38f)

~~A160-A159.~~ In addition to the sources of information indicated in paragraph 38f, other relevant information may include the following:

- Information communicated by the firm's network in accordance with paragraphs 51c and 52b about the firm's system of quality management, including the network requirements or network services that the firm has included in its system of quality management
- Information communicated by a service provider about the resources the firm uses in its system of quality management
- Information from regulators about the entities for whom the firm performs engagements, which is made available to the firm, such as information from a securities regulator about an entity for whom the firm performs engagements (for example, irregularities in the entity's financial statements)

Commented [AG30]: Sara: Can we ask ASB if it would change anything if these words were deleted?

~~A161-A160.~~ The results of external inspections or other relevant information, both internal and external, may indicate that previous monitoring activities undertaken by the firm failed to identify a deficiency in the system of quality management. This information may affect the firm's consideration of the nature, timing, and extent of the monitoring activities.

~~A162-A161.~~ External inspections are not a substitute for the firm's internal monitoring activities. Nevertheless, the results of external inspections inform the nature, timing, and extent of the monitoring activities.

Engagement Inspections (Ref: par. 39)

~~A163-A162.~~ Examples of matters in paragraph 38 that may be considered by the firm in selecting completed engagements for inspection include the following:

- In relation to the conditions, events, circumstances, actions, or inactions giving rise to the quality risks:
 - The types of engagements performed by the firm, and the extent of the firm’s experience in performing the type of engagement
 - The types of entities for which engagements are undertaken, for example: such as the following:
 - Entities operating in emerging industries
 - Entities operating in industries associated with a high level of complexity or judgment
 - Entities operating in an industry that is new to the firm
 - The tenure and experience of engagement partners
- The results of previous inspections of completed engagements, including for each engagement partner
- In relation to other relevant information:
 - Complaints or allegations about an engagement partner
 - The results of external inspections, including for each engagement partner
 - The results of the firm’s evaluation of each engagement partner’s commitment to quality

A164-A163. The firm may undertake multiple monitoring activities, other than inspection of completed engagements, that focus on determining whether engagements have complied with policies or procedures. These monitoring activities may be undertaken on certain engagements or engagement partners. The nature and extent of these monitoring activities, and the results, may be used by the firm in determining the following:

- How often to select completed engagements for inspection, and which completed engagements to select, based on the factors described in paragraph A159
- Which engagement partners to select for inspection, and how frequently to select an engagement partner for inspection, based on factors such as how long it has been since the engagement partner was subject to inspection, the results of previous inspections of the engagement partner, or the engagement partner’s experience with performing engagements at different levels of service, in new industries, or with complex financial reporting matters
- Which aspects of the engagement to consider when performing the inspection of completed engagements

For example, if the firm has undertaken inspections of in-process engagements,

- the firm may determine it appropriate to reduce the extent of selection of completed engagements for inspection;
- the results of the inspections of in-process engagements may indicate areas of risk that may affect which completed engagements are selected for inspection; or

- the results of the inspections of in-process engagements may identify negative quality issues that prompt the firm to shorten the inspection cycle or expand the extent of completed engagement inspections.

~~A165-A164.~~ The inspection of completed engagements for engagement partners on a cyclical basis may assist the firm in monitoring whether engagement partners have fulfilled their overall responsibility for managing and achieving quality on the engagements to which they are assigned.

~~A166-A165.~~ Examples of policies and procedures that a firm may establish to apply a cyclical basis for the inspection of completed engagements for each engagement partner include the following policies or procedures that

- set forth the standard period of the inspection cycle, such as the inspection of a completed engagement for each engagement partner performing audits of financial statements once every, for example, three years, and for all other engagement partners, once every, for example, five years.
- set out the criteria for selecting completed engagements, including that for an engagement partner performing audits of financial statements, the engagements selected include an audit engagement.
- address the selection of engagement partners in a manner that is unpredictable.
- address when it is necessary or appropriate to select engagement partners more, or less, frequently than the standard period set out in the policy. Examples follow:

— The firm may select engagement partners more frequently than the standard period set out in the firm's policy when the following apply:

- ~~multiple~~Multiple deficiencies have been identified by the firm that have been evaluated as severe, and the firm determines that a more frequent cyclical inspection is needed across all engagement partners-
- ~~the~~The engagement partner performs engagements for entities operating in a certain industry in which there are high levels of complexity or judgment-
- ~~an~~An engagement performed by the engagement partner has been subject to other monitoring activities, and the results of the other monitoring activities were unsatisfactory-
- ~~the~~The engagement partner has performed an engagement for an entity operating in an industry in which the engagement partner has limited experience-
- ~~the~~The engagement partner has limited experience in performing that level of service engagements-
- ~~the~~The engagement partner is a newly appointed engagement partner or has recently joined the firm from another firm or another jurisdiction-

— The firm may defer the selection of the engagement partner (for example, deferring for a year beyond the standard period set out in the firm's policy) when

- engagements performed by the engagement partner have been subject to other monitoring activities during the standard period set out in the firm's policy, and

- the results of the other monitoring activities provide sufficient information about the engagement partner; that is, performing the inspection of completed engagements would unlikely provide the firm with further information about the engagement partner.

~~A167-A166.~~ The matters considered in an inspection of an engagement depend on how the inspection will be used to monitor the system of quality management. Ordinarily, the inspection of an engagement includes determining that responses that are implemented at the engagement level (for example, the firm’s policies and procedures in respect of engagement performance) have been implemented as designed and are operating effectively.

The Relationship of Peer Review to Monitoring

~~A168-A167.~~ A peer review is not a substitute for all monitoring activities. However, because the objective of a peer review is similar to that of an inspection, the firm’s quality management policies or procedures may provide that a peer review conducted under standards established by the AICPA may be a substitute for the inspection of engagement documentation, reports, and clients’ financial statements for some or all engagements for the period covered by the peer review.

~~A169-A168.~~ ~~A167A.~~ A peer review may result in findings or deficiencies. However, the definitions of *findings* and *deficiencies* in this SQMS are different than the definitions of those terms in *AICPA Standards for Performing and Reporting on Peer Reviews*.⁷ Accordingly, findings and deficiencies may be evaluated differently for peer review purposes than for purposes of this SQMS. Findings or deficiencies identified in a firm’s system of quality management may not necessarily result in a peer review finding or deficiency; similarly, peer review findings or deficiencies may not necessarily equate to findings or deficiencies in a firm’s system of quality management. As with other items identified in the firm’s monitoring activities, the firm would need to assess any peer review findings or deficiencies to determine the impact on the firm’s evaluation of its system of quality management.

Commented [AG31]: Should be footnote number 17

Individuals Performing the Monitoring Activities (Ref: par. ~~40b40~~)

~~A170-A169.~~ It is important that individuals performing the monitoring activities have the competence, capabilities, time, and objectivity to perform the monitoring activities. Each of these attributes is equally essential. In some circumstances, there may not be personnel who have the competence, capabilities, time, and objectivity to perform the monitoring activities. In these circumstances, the firm may use network services or a service provider to perform the monitoring activities.

Commented [AG32]: Revisions in this sections were directed by the ASB in January

~~A171-A170.~~ The provisions of relevant ethical requirements are relevant in designing the policies or procedures addressing the objectivity of the individuals performing the monitoring activities. A self-review threat may arise when an individual who performs an inspection of an engagement was an engagement team member or the engagement quality reviewer of that engagement. A self-review threat may also arise when an individual ~~who participated~~ involved in

⁷ Paragraphs 70 and 110, PRP section 1000, *AICPA Standards for Performing and Reporting on Peer Reviews* (AICPA, *Professional Standards*).

~~operating~~ the response to a quality risk; is performing the monitoring of that response. For example, a self-review threat may arise if an engagement partner who is responsible for ~~client acceptance at the engagement level or at the firm level~~ accepting their own client engagements is also responsible for monitoring compliance with the firm's client acceptance policies and procedures.

~~A172.A171. In some circumstances, for example, in the case of a less complex firm, there may not be personnel who have the competence, capabilities, time, or objectivity to perform the monitoring activities. In these circumstances, the firm may use network services or a service provider to perform the monitoring activities.~~ This SQMS does not preclude an individual from performing monitoring activities, including inspections, of their own compliance with a quality management system. However, such self-inspections may be less effective than compliance inspections by another qualified individual. When an individual inspects their own compliance with the firm's policies and procedures, the firm has a higher risk that noncompliance with policies and procedures will not be detected or reported. To effectively monitor one's own compliance, it is necessary that an individual be able to critically review their own performance, assess their own strengths and weaknesses, and maintain an attitude of continual improvement.

~~A173.A172.~~ Responses that may provide safeguards against the self-review threat and lessen the likelihood of deficiencies in the system of quality management include the following actions:

- Fostering a commitment to continuing professional education and providing effective training programs so that personnel stay current on accounting, auditing, and quality management standards
- Providing training on how to perform monitoring inspections and requiring the use of peer review or other inspection checklists
- Requiring the passage of time after the completion of an engagement before self-inspections are performed

~~A174.A173. A170A.~~ The firm may have responses in place to address ~~other~~ quality risks other than the self-review threat that may be particularly helpful when self-inspections are performed, such as the following actions:

- Establishing strong client acceptance and engagement continuance policies that ~~provide reasonable assurance that~~ address the risk of the firm ~~doesn't accept~~ accepting or ~~retain~~ continuing engagements it doesn't have the competency and resources to perform
- Establishing consultation policies that ~~provide reasonable assurance~~ require engagement teams ~~will~~ to consult when they encounter technical accounting and auditing difficulties
- Taking corrective action in response to the results identified by the firm's internal monitoring, engagement quality reviews, peer review results or other external inspections; for example, inspections by the U.S. Department of Labor
- Requiring the use of an external service provider to perform engagement quality reviews or monitoring ~~procedures~~ activities when
 - deficiencies identified by the firm's monitoring activities, peer reviewers or other external inspections indicate that self-inspection is not effective, or
 - changes in conditions and the environment within the firm (such as obtaining clients in an industry not previously serviced or significantly changing the size of the firm) occur.

Evaluating Findings and Identifying Deficiencies (Ref: par. 17 and 41–42)

~~A175-A174.~~ The firm accumulates findings from the performance of monitoring activities, external inspections, and other relevant sources. Information accumulated by the firm from the monitoring activities, external inspections, and other relevant sources may reveal other observations about the firm’s system of quality management, such as

- actions, behaviors, or conditions that have given rise to positive outcomes in the context of quality or the effectiveness of the system of quality management, or
- similar circumstances in which no findings were noted (for example, engagements in which no findings were noted, and the engagements have a similar nature to the engagements in which findings were noted).

Other observations may be useful to the firm because they may assist the firm in investigating the root causes of identified deficiencies, indicate practices that the firm can support or apply more extensively (for example, across all engagements), or highlight opportunities for the firm to enhance the system of quality management.

~~A176-A175.~~ The firm exercises professional judgment in determining whether findings, individually or in combination with other findings, give rise to a deficiency in the system of quality management. In making the judgment, the firm may need to take into account the relative importance of the findings in the context of the quality objectives, quality risks, responses, or other aspects of the system of quality management to which they relate. The firm’s judgments may be affected by quantitative and qualitative factors relevant to the findings. In some circumstances, the firm may determine it appropriate to obtain more information about the findings in order to determine whether a deficiency exists. Not all findings, including engagement findings, will be a deficiency.

~~A177-A176.~~ Examples of quantitative and qualitative factors that a firm may consider in determining whether findings give rise to a deficiency include the following:

Quality risks and responses

- **If the findings relate to a response, factors such as the following:**
 - How the response is designed; for example, the nature of the response, the frequency of its occurrence (if applicable), and the relative importance of the response to addressing the quality risks and achieving the quality objectives to which it relates
 - The nature of the quality risk to which the response relates and the extent to which the findings indicate that the quality risk has not been addressed
 - Whether there are other responses that address the same quality risk and whether there are findings for those responses

Commented [ACR33]: Is there way to use an introduction such as “the following may be considered”

Nature of the findings and their pervasiveness

- The nature of the findings. ~~For~~ **for** example, findings related to leadership actions and behaviors may be qualitatively significant, given the pervasive effect this could have on the system of quality management as a whole.

- Whether the findings, in combination with other findings, indicate a trend or systemic issue. ~~For; for~~ example, similar engagement findings that appear on multiple engagements may indicate a systemic issue.

Extent of Monitoring Activity and Extent of Findings

- The extent of the monitoring activity from which the findings arose, including the number or size of the selections.
- The extent of the findings in relation to the selection covered by the monitoring activity and in relation to the expected deviation rate. ~~For; for~~ example, in the case of inspection of engagements, the number of engagements selected in which the findings were identified, relative to the total number of engagements selected, and the expected deviation rate set by the firm.

~~A178-A177.~~ Evaluating findings and identifying deficiencies and evaluating the severity and pervasiveness of an identified deficiency, including investigating the root causes of an identified deficiency, are part of an iterative and nonlinear process. Examples ~~follows~~ follow:

- In investigating the root causes of an identified deficiency, the firm may identify a circumstance that has similarities to other circumstances in which there were findings that were not considered deficiencies. As a result, the firm adjusts its evaluation of the other findings and classifies them as deficiencies.
- In evaluating the severity and pervasiveness of an identified deficiency, the firm may identify a trend or systemic issue that correlates with other findings that are not considered deficiencies. As a result, the firm adjusts its evaluation of the other findings and also classifies them as deficiencies.

~~A179-A178.~~ The results of monitoring activities, results of external inspections, and other relevant information (for example, network monitoring activities or complaints and allegations) may reveal information about the effectiveness of the monitoring and remediation process. For example, the results of external inspections may provide information about the system of quality management that has not been identified by the firm's monitoring and remediation process, which may highlight a deficiency in that process.

Evaluating Identified Deficiencies (Ref: par. 42)

~~A180-A179.~~ Factors the firm may consider in evaluating the severity and pervasiveness of an identified deficiency include the following:

- The nature of the identified deficiency, including the aspect of the firm's system of quality management to which the deficiency relates, and whether the deficiency is in the design, implementation, or operation of the system of quality management
- In the case of identified deficiencies related to responses, whether there are compensating responses to address the quality risk to which the response relates
- The root causes of the identified deficiency
- The frequency with which the matter giving rise to the identified deficiency occurred

- The magnitude of the identified deficiency, how quickly it occurred, and the duration of time that it existed and had an effect on the system of quality management

~~A181~~A180. The severity and pervasiveness of identified deficiencies affects the evaluation of the system of quality management that is undertaken by the individual or individuals assigned ultimate responsibility and accountability for the system of quality management.

Root Cause of the Identified Deficiencies (Ref: par. 42a)

~~A182~~A181. The objective of investigating the root causes of identified deficiencies is to understand the underlying circumstances that caused the deficiencies to enable the firm to

- evaluate the severity and pervasiveness of the identified deficiency and
- appropriately remediate the identified deficiency.

Performing a root cause analysis involves the exercise of professional judgment based on the evidence available by those performing the assessment.

~~A183~~A182. The nature, timing, and extent of the procedures undertaken to understand the root causes of an identified deficiency may also be affected by the nature and circumstances of the firm, such as the following:

- The complexity and operating characteristics of the firm.
- The size of the firm.
- The geographical dispersion of the firm.
- How the firm is structured or the extent to which the firm concentrates or centralizes its processes or activities. For example, in the case of a less complex firm with a single location, the firm's procedures to understand the root causes of a deficiency may be simple because the information to inform the understanding may be readily available and concentrated, and the root causes may be more apparent. In the case of a more complex firm with multiple locations, the procedures to understand the root causes of a deficiency may include using individuals specifically trained on investigating the root causes of identified deficiencies and developing a methodology with more formalized procedures for identifying root causes.
- The nature of the identified deficiency; for example, the firm's procedures to understand the root causes of an identified deficiency may be more rigorous in circumstances when an engagement report related to an audit of financial statements was issued that was inappropriate, or the identified deficiency relates to leadership's actions and behaviors regarding quality.
- The possible severity of the identified deficiency; for example, the firm's procedures to understand the root causes of an identified deficiency may be more rigorous in circumstances ~~when-in which~~ the deficiency has been identified across multiple engagements, or there is an indication that policies or procedures have high rates of noncompliance.

~~A184~~A183. In investigating the root causes of identified deficiencies, the firm may consider why deficiencies did not arise in other circumstances that are of a similar nature to the matter to

which the identified deficiency relates. Such information may also be useful in determining how to remediate an identified deficiency. For example, the firm may determine that a deficiency exists because similar findings have occurred across multiple engagements. However, the findings have not occurred in several other engagements within the same population being tested. By contrasting the engagements, the firm concludes that the root cause of the identified deficiency is a lack of appropriate involvement by the engagement partners at key stages of the engagements.

~~A185-A184.~~ Identifying root causes that are appropriately specific may support the firm's process for remediating identified deficiencies. For example, the firm may identify that engagement teams performing audits of financial statements are failing to obtain sufficient appropriate audit evidence on accounting estimates when management's assumptions have a high degree of subjectivity. Although the firm notes that these engagement teams are not maintaining appropriate professional skepticism, the underlying root cause of this issue may relate to another matter, such as a cultural environment that does not encourage engagement team members to question individuals with greater authority or insufficient direction, supervision, and review of the work performed on the engagements.

~~A186-A185.~~ In addition to investigating the root causes of identified deficiencies, the firm may also investigate the root causes of positive outcomes because doing so may reveal opportunities for the firm to improve, or further enhance, the system of quality management.

Responding to Identified Deficiencies (Ref: par. 43)

~~A187-A186.~~ The nature, timing, and extent of remedial actions may depend on a variety of other factors, including the following:

- The root causes
- The severity and pervasiveness of the identified deficiency and, therefore, the urgency with which it needs to be addressed
- The effectiveness of the remedial actions in addressing the root causes, such as whether the firm needs to implement more than one remedial action in order to effectively address the root causes, or needs to implement remedial actions as interim measures until the firm is able to implement more effective remedial actions

~~A188-A187.~~ In some circumstances, the remedial action may include establishing additional quality objectives, or quality risks or responses may be added or modified, because it is determined that they are not appropriate.

~~A189-A188.~~ In circumstances ~~whenin which~~ the firm determines that the root cause of an identified deficiency relates to a resource provided by a service provider, the firm may also

- consider whether to continue using the resource provided by the service provider, ~~or~~
- communicate the matter to the service provider.

The firm is responsible for addressing the effect of the identified deficiency related to a resource provided by a service provider on the system of quality management and taking action to prevent the deficiency from recurring with respect to the firm's system of quality management. However, the firm is not ordinarily responsible for remediating the identified deficiency on behalf of the service provider or further investigating the root cause of the identified deficiency at the service provider.

Findings About a Particular Engagement (Ref: par. 46)

~~A190-A189.~~ AU-C section 585, *Consideration of Omitted Procedures After the Report Release Date*, addresses the auditor's responsibilities in circumstances ~~in which when~~ procedures were omitted, or the report issued is inappropriate. In such circumstances relating to other assurance and attest engagements, the action taken by the firm may include the following:

- Consulting with appropriate individuals regarding the appropriate action
- Discussing the matter with management of the entity or those charged with governance
- Performing the omitted procedures

The actions taken by the firm do not relieve the firm of the responsibility to take further actions relating to the finding in the context of the system of quality management, including evaluating the findings to identify deficiencies and, when a deficiency exists, investigating the root causes of the identified deficiency.

Ongoing Communication Related to the Monitoring and Remediation (Ref: par. 47)

~~A191-A190.~~ The information communicated about the monitoring and remediation to the individual or individuals assigned ultimate responsibility and accountability for the system of quality management may be communicated on an ongoing basis or periodically. The individual or individuals may use the information in multiple ways. Examples follow:

- As a basis for further communications to personnel about the importance of quality
- To hold individuals accountable for their roles assigned to them
- To identify key concerns about the system of quality management in a timely manner

The information also provides a basis for the evaluation of the system of quality management, and conclusion thereon, as required by paragraphs 54–56.

Network Requirements or Network Services (Ref: par. 49)

~~A192-A191.~~ In some circumstances, the firm may belong to a network. Networks may establish requirements regarding the firm's system of quality management or may make services or resources available that the firm may choose to implement or use in the design, implementation, and operation of its system of quality management. Such requirements or services may be intended to promote the consistent performance of quality engagements across the firms that belong to the network. The extent to which the network will provide the firm with quality objectives, quality risks, and responses that are common across the network will depend on the firm's arrangements with the network.

~~A193-A192.~~ Examples of network requirements include the following:

- Requirements for the firm to include additional quality objectives or quality risks in the firm's system of quality management that are common across the network firms.
- Requirements for the firm to include responses in the firm's system of quality management that are common across the network firms. Such responses designed by the network may include network policies or procedures that specify the leadership roles and responsibilities, including how the firm is expected to assign authority and responsibility

within the firm, or resources, such as network-developed methodologies for performing engagements or IT applications.

- Requirements that the firm be subject to the network’s monitoring activities. These monitoring activities may relate to network requirements (for example, monitoring that the firm has implemented the network’s methodology appropriately) or to the firm’s system of quality management in general.

A194-A193. Examples of network services include services or resources that are optional for the firm to use in its system of quality management or in performing engagements, such as voluntary training programs, use of component auditors or specialists from within the network, or use of a service delivery center established at the network level, or by another network firm or group of network firms.

A195-A194. The network may establish responsibilities for the firm in implementing the network requirements or network services. Examples follow:

- The firm is required to have certain IT infrastructure and IT processes in place to support an IT application provided by the network that the firm uses in the system of quality management.
- The firm is required to provide firm-wide training on the methodology provided by the network, including when updates are made to the methodology.

A196-A195. The firm’s understanding of the network requirements or network services and the firm’s responsibilities relating to the implementation thereof may be obtained through inquiries of, or documentation provided by, the network about matters such as the following:

- The network’s governance and leadership
- The procedures undertaken by the network in designing, implementing, and, if applicable, operating, the network requirements or network services
- How the network identifies and responds to changes that affect the network requirements or network services or other information, such as changes in the professional standards or information that indicates a deficiency in the network requirements or network services
- How the network monitors the appropriateness of the network requirements or network services, which may include through the network firms’ monitoring activities, and the network’s processes for remediating identified deficiencies

Network Requirements or Network Services in the Firm’s System of Quality Management
(Ref: par. 50)

A197-A196. The characteristics of the network requirements or network services are a condition, event, circumstance, action, or inaction in identifying and assessing quality risks. An example of a network requirement or network service that gives rise to a quality risk is as follows.

The network may require the firm to use an IT application for the acceptance and continuance of client relationships and specific engagements that is standardized across the network. This may give rise to a quality risk that the IT application does not address matters in local law or regulation

that need to be considered by the firm in accepting and continuing client relationships and specific engagements.

A198, A197. The purpose of the network requirements may include the promotion of consistent performance of quality engagements across the network firms. The firm may be expected by the network to implement the network requirements; however, the firm may need to adapt or supplement the network requirements such that they are appropriate for the nature and circumstances of the firm and its engagements.

A199, A198. Examples of how the network requirements or network services may need to be adapted or supplemented include the following:

<i>Network requirement or network service</i>	<i>How the firm adapts or supplements the network requirement or network service</i>
<p>The network requires the firm to include certain quality risks in the system of quality management, so that all firms in the network address the quality risks. The network does not provide an assessment of the quality risks.</p>	<p>As part of identifying and assessing quality risks, the firm assesses the quality risks that are required by the network.</p> <p>The firm also designs and implements responses to address the assessed quality risks that are required by the network.</p>
<p>The network requires that the firm design and implement certain responses.</p>	<p>As part of designing and implementing responses, the firm determines</p> <ul style="list-style-type: none"> • which assessed quality risks the responses address. • how the responses required by the network will be incorporated into the firm’s system of quality management, given the nature and circumstances of the firm. This may include tailoring the response to reflect the nature and circumstances of the firm and the engagements performed by the firm (for example, tailoring a methodology to include matters related to law or regulation).

<p>The firm uses individuals from other network firms as component auditors. Network requirements are in place that drive a high degree of commonality across the network firms' systems of quality management. The network requirements include specific criteria that apply to individuals assigned to work on a component for a group audit.</p>	<p>The firm establishes policies or procedures that require the engagement team to confirm with the component auditor (that is, the other network firm) that the individuals assigned to the component meet the specific criteria set out in the network requirements.</p>
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A200-A199. In some circumstances, in adapting or supplementing the network requirements or network services, the firm may identify possible improvements to the network requirements or network services and may communicate these improvements to the network.

Monitoring Activities Undertaken by the Network on the Firm's System of Quality Management (Ref: par. 51c)

A201-A200. The results of the network's monitoring activities of the firm's system of quality management may include information such as the following:

- A description of the monitoring activities, including their nature, timing, and extent
- Findings, identified deficiencies, and other observations about the firm's system of quality management (for example, positive outcomes or opportunities for the firm to improve, or further enhance, the system of quality management)
- The network's evaluation of the root causes of the identified deficiencies, the assessed effect of the identified deficiencies, and recommended remedial actions

Monitoring Activities Undertaken by the Network Across the Network Firms (Ref: par. 52b)

A202-A201. The information from the network about the overall results of the network's monitoring activities undertaken across the network firms' systems of quality management may be an aggregation or summary of the information described in paragraph A193, including trends and common areas of identified deficiencies across the network, or positive outcomes that may be replicated across the network. Such information may

- be used by the firm
 - in identifying and assessing quality risks, ~~and~~
 - as part of other relevant information considered by the firm in determining whether deficiencies exist in the network requirements or network services used by the firm in its system of quality management.
- be communicated to group engagement partners, in the context of considering the competence and capabilities of component auditors from a network firm who are

subject to common network requirements (for example, common quality objectives, quality risks, and responses).

~~A203~~A202. In some circumstances, the firm may obtain information from the network about deficiencies identified in a network firm's system of quality management that affects the firm. The network may also gather information from network firms regarding the results of external inspections over network firms' systems of quality management. In some instances, law or regulation in a particular jurisdiction may prevent the network from sharing information with other network firms or may restrict the specificity of such information.

~~A204~~A203. In circumstances when in which the network does not provide the information about the overall results of the network's monitoring activities across the network firms, the firm may take further actions, such as

- discussing the matter with the network, and
- determining the effect on the firm's engagements and communicating the effect to engagement teams.

Deficiencies in Network Requirements or Network Services Identified by the Firm (Ref: par. 53)

~~A205~~A204. As network requirements or network services used by the firm form part of the firm's system of quality management, they are also subject to the requirements of this SQMS regarding monitoring and remediation. The network requirements or network services may be monitored by the network, the firm, or a combination of both; for example, a network may undertake monitoring activities at a network level for a common methodology. The firm may also monitor the application of the methodology by engagement team members through performing engagement inspections.

~~A206~~A205. In designing and implementing the remedial actions to address the effect of the identified deficiency in the network requirements or network services, the firm may

- understand the planned remedial actions by the network, including whether the firm has any responsibilities for implementing the remedial actions, and
- consider whether supplementary remedial actions need to be taken by the firm to address the identified deficiency and the related root causes, such as when
 - the network has not taken appropriate remedial actions, or
 - the network's remedial actions will take time to effectively address the identified deficiency.

Evaluating the System of Quality Management (Ref: par. 54)

~~A207~~A206. The individual or individuals assigned ultimate responsibility and accountability for the system of quality management may be assisted by other individuals in performing the evaluation. Nevertheless, the individual or individuals assigned ultimate responsibility and accountability for the system of quality management remain responsible and accountable for the evaluation.

~~A208-A207.~~ The point in time at which the evaluation is undertaken may depend on the circumstances of the firm and may coincide with the fiscal year-end of the firm or the completion of an annual monitoring cycle.

~~A209-A208.~~ The information that provides the basis for the evaluation of the system of quality management includes the information communicated to the individuals assigned ultimate responsibility and accountability for the system of quality management in accordance with paragraph 47.

~~A210-A209.~~ An example of scalability to demonstrate how the information that provides the basis for the evaluation of the system of quality management may be obtained in firms of different complexity is as follows:

- In a less complex firm, the individual or individuals assigned ultimate responsibility and accountability for the system of quality management may be directly involved in the monitoring and remediation and, therefore, will be aware of the information that supports the evaluation of the system of quality management.
- In a more complex firm, the individual or individuals assigned ultimate responsibility and accountability for the system of quality management may need to establish processes to collate, summarize, and communicate the information needed to evaluate the system of quality management.

Concluding on the System of Quality Management (Ref: par. 55)

~~A211-A210.~~ In the context of this SQMS, it is intended that the operation of the system as a whole provides the firm with reasonable assurance that the objectives of the system of quality management are being achieved. In concluding on the system of quality management, the individual or individuals assigned ultimate responsibility and accountability for the system of quality management may, in using the results of the monitoring and remediation process, consider the following:

- The severity and pervasiveness of identified deficiencies and the effect on the achievement of the objectives of the system of quality management
- Whether remedial actions have been designed and implemented by the firm and whether the remedial actions taken up to the time of the evaluation are effective
- Whether the effect of identified deficiencies on the system of quality management have been appropriately corrected, such as whether further actions have been taken in accordance with paragraph 46

~~A212-A211.~~ There may be circumstances when in which identified deficiencies that are severe (including identified deficiencies that are severe and pervasive) have been appropriately remediated and the effect of them corrected at the point in time of the evaluation. In such cases, the individual or individuals assigned ultimate responsibility and accountability for the system of quality management may conclude that the system of quality management provides the firm with reasonable assurance that the objectives of the system of quality management are being achieved.

~~A213.~~A212. An identified deficiency may have a pervasive effect on the design, implementation, and operation of the system of quality management when, for example, ~~the~~ following apply:

- ~~the~~The deficiency affects several components or aspects of the system of quality management.
- ~~the~~The deficiency is confined to a specific component or aspect of the system of quality management but is fundamental to the system of quality management.
- ~~the~~The deficiency affects several business units or geographical locations of the firm.
- ~~the~~The deficiency is confined to a business unit or geographical location, but the business unit or location affected is fundamental to the firm overall.
- ~~the~~The deficiency affects a substantial portion of engagements that are of a certain type or nature.

~~A214.~~A213. An example of an identified deficiency that may be considered severe but not pervasive is as follows:

The firm identifies a deficiency in one of its smaller regional offices. The identified deficiency relates to noncompliance with many firm policies or procedures. The firm determines that the culture in the regional office, particularly the actions and behavior of leadership in the regional office, which were overly focused on financial priorities, has contributed to the root cause of the identified deficiency. The firm determines that the effect of the identified deficiency is as follows:

- Severe, because it relates to the culture of the regional office and overall compliance with firm policies or procedures
- Not pervasive, because it is limited to the smaller regional office

~~A215.~~A214. The individual or individuals assigned ultimate responsibility and accountability for the system of quality management may conclude that the system of quality management does not provide the firm with reasonable assurance that the objectives of the system of quality management are being achieved in circumstances ~~when~~ in which identified deficiencies are severe and pervasive, actions taken to remediate the identified deficiencies are not appropriate, and the effect of the identified deficiencies have not been appropriately corrected.

~~A216.~~A215. An example of an identified deficiency that may be considered severe and pervasive is as follows:

The firm identifies a deficiency in a regional office, which is the firm's largest office and provides financial, operational, and technical support for the entire region. The identified deficiency relates to noncompliance with many firm policies or procedures. The firm determines that the culture in the regional office, particularly the actions and behavior of leadership in the regional office, which were overly focused on financial priorities, has contributed to the root cause of the identified deficiency. The firm determines that the effect of the identified deficiency is as follows:

- Severe, because it relates to the culture of the regional office and overall compliance with firm policies or procedures
- Pervasive, because the regional office is the largest office and provides support to many other offices, and the noncompliance with firm policies or procedures may have had a broader effect on the other offices

~~A217-A216.~~ It may take time for the firm to remediate identified deficiencies that are severe and pervasive. As the firm continues to take action to remediate the identified deficiencies, the pervasiveness of the identified deficiencies may be diminished, and it may be determined that the identified deficiencies are still severe but no longer severe and pervasive. In such cases, the individual or individuals assigned ultimate responsibility and accountability for the system of quality management may conclude that, except for matters related to identified deficiencies that have a severe but not pervasive effect on the design, implementation, and operation of the system of quality management, the system of quality management provides the firm with reasonable assurance that the objectives of the system of quality management are being achieved.

~~A218-A217.~~ This SQMS does not require the firm to obtain an independent ~~assurance report~~ ~~evaluation~~ (for example, a peer review ~~or SOC~~ report) on its system of quality management annually or preclude the firm from doing so.

Taking Prompt and Appropriate Action and Further Communication (Ref: par. 56)

~~A219-A218.~~ In circumstances ~~whenin which~~ the individual or individuals assigned ultimate responsibility and accountability for the system of quality management reach the conclusion described in paragraph 54b or 54c, the prompt and appropriate action taken by the firm may include the following:

- Taking measures to support performing engagements through assigning more resources or developing more guidance and to confirm that reports issued by the firm are appropriate in the circumstances, until such time as the identified deficiencies are remediated, and communicating such measures to engagement teams
- Obtaining legal advice

~~A220-A219.~~ In some circumstances, the firm may have an independent governing body that has nonexecutive oversight of the firm. In such circumstances, communications may include informing the independent governing body.

~~A221-A220.~~ Examples of circumstances in which it may be appropriate for the firm to communicate to external parties about the evaluation of the system of quality management include the following:

- When the firm belongs to a network
- When other network firms use the work performed by the firm, for example, in the case of a group audit
- When a report issued by the firm is determined by the firm to be inappropriate as a result of the failure of the system of quality management, and management or those charged with governance of the entity need to be informed

- When law or regulation requires the firm to communicate to an oversight authority or a regulatory body

Performance Evaluations (Ref: par. 57)

A222-A221. Periodic performance evaluations promote accountability. In considering the performance of an individual, the firm may take the following into account:

- The results of the firm’s monitoring activities for aspects of the system of quality management that relate to the responsibility of the individual. In some circumstances, the firm may set targets for the individual and measure the results of the firm’s monitoring activities against those targets.
- The actions taken by the individual in response to identified deficiencies that relate to the responsibility of that individual, including the timeliness and effectiveness of such actions.

A223-A222. An example of scalability to demonstrate how firms of different complexity may undertake the performance evaluations is as follows:

- In a less complex firm, the firm may engage a service provider to perform the evaluation, or the results of the firm’s monitoring activities may provide an indication of the performance of the individual.
- In a more complex firm, the performance evaluations may be undertaken by an independent nonexecutive member of the firm’s governing body or a special committee overseen by the firm’s governing body.

A224-A223. A positive performance evaluation may be rewarded through compensation, promotion, and other incentives that focus on the individual’s commitment to quality and reinforce accountability. On the other hand, the firm may take corrective actions to address a negative performance evaluation that may affect the firm’s achievement of its quality objectives.

Documentation (Ref: par. 58–60)

A225-A224. Documentation provides evidence that the firm complies with this SQMS, as well as law, regulation, or relevant ethical requirements. It may also be useful for training personnel and engagement teams, ensuring the retention of organizational knowledge, and providing a history of the basis for decisions made by the firm about its system of quality management. It is neither necessary nor practicable for the firm to document every matter considered, or judgment made, about its system of quality management. Furthermore, compliance with this SQMS may be evidenced by the firm through its information and communication component, documents or other written materials, or IT applications that are integral to the components of the system of quality management.

A226-A225. Documentation may be formal (for example, written manuals, checklists, and forms), informal (for example, email communication or postings on websites), or held in IT applications or other digital forms (for example, in databases). Factors that may affect the firm’s judgments about the form, content, and extent of documentation, including how often documentation is updated, may include the following:

- The complexity of the firm and the number of offices
- The nature and complexity of the firm’s practice and organization
- The nature of engagements the firm performs and the nature of the entities for whom engagements are performed
- The nature and complexity of the matter being documented, such as whether it relates to an aspect of the system of quality management that has changed or an area of greater quality risk, and the complexity of the judgments relating to the matter
- The frequency and extent of changes in the system of quality management

In a less complex firm, it may not be necessary to have documentation supporting matters communicated because informal communication methods may be effective. Nevertheless, a less complex firm may determine it appropriate to document such communications in order to provide evidence that they occurred.

~~A227~~,A226. In some instances, an external oversight authority may establish documentation requirements, either formally or informally, for example, as a result of the outcome of external inspection findings. Relevant ethical requirements may also include specific requirements addressing documentation; for example, the AICPA code requires documentation of particular matters, including certain situations related to conflicts of interest, noncompliance with laws and regulations, and independence.

~~A228~~,A227. The firm is not required to document the consideration of every condition, event, circumstance, action, or inaction for each quality objective or each risk that may give rise to a quality risk. However, in documenting the quality risks and how the firm’s responses address the quality risks, the firm may document the reasons for the assessment given to the quality risks (that is, the considered occurrence and effect on the achievement of one or more quality objectives) to support the consistent implementation and operation of the responses.

~~A229~~,A228. The documentation may be provided by the network, other network firms, or other structures or organizations within the network.



ASB Meeting
May 11-12, 2022
Agenda Item 2B

STATEMENT ON QUALITY MANAGEMENT STANDARDS
ENGAGEMENT QUALITY REVIEWS

Commented [AG1]: Note: For ease of reading and to speed the turnaround and issuance of the final standard, the word "proposed" has been added as a watermark, deleted from the text and not shown in track changes; and references have been updated to refer to SQMS No. 1 and SAS No. 146.

Proposed

CONTENTS

	Paragraph
Introduction	
Scope of this SQMS	1-4
The Firm's System of Quality Management and Role of Engagement Teams	5-9
Authority of this SQMS	10
Effective Date	11
Objective	12
Definitions	13
Requirements	
Applying, and Complying With, Relevant Requirements	14-16
Appointment and Eligibility of Engagement Quality Reviewers	17-23
Performance of the Engagement Quality Review	24-27
Documentation	28-30
Application and Other Explanatory Material	
Appointment and Eligibility of Engagement Quality Reviewers	A1-A27
Performance of the Engagement Quality Review	A28-A50
Documentation	A51-A54

Introduction

Scope of This Statement on Quality Management Standards

1. This Statement on Quality Management Standards (SQMS) addresses the following:
 - a. The appointment and eligibility of the engagement quality reviewer
 - b. The engagement quality reviewer's responsibilities relating to the performance and documentation of an engagement quality review
2. This SQMS applies to all engagements for which an engagement quality review is required to be performed in accordance with SQMS No. 1, *A Firm's System of Quality Management*, including when the firm has determined that an engagement quality review is an appropriate response to assessed quality risks.¹ This SQMS is to be read in conjunction with the AICPA Code of Professional Conduct (AICPA code) and other relevant ethical requirements.
3. An engagement quality review performed in accordance with this SQMS is a specified response that is designed and implemented by the firm in accordance with SQMS No. 1.² The performance of an engagement quality review is undertaken at the engagement level by the engagement quality reviewer on behalf of the firm.

Scalability

4. The nature, timing, and extent of the engagement quality reviewer's procedures required by this SQMS vary depending on the nature and circumstances of the engagement or the entity. For example, for engagements involving fewer significant judgments made by the engagement team, the engagement quality reviewer's procedures would likely be less extensive.

The Firm's System of Quality Management and Role of Engagement Quality Reviews

5. SQMS No. 1 establishes the firm's responsibilities for its system of quality management and requires the firm to design and implement responses to address the quality risks in a manner that is based on, and responsive to, the reasons for the assessments given to the quality risks.³ The specified responses in SQMS No. 1⁴ include establishing policies or procedures addressing engagement quality reviews in accordance with this SQMS.
6. The firm is responsible for designing, implementing, and operating the system of quality management. Under SQMS No. 1, the objective of the firm is to design, implement, and operate a system of quality management for engagements performed by the firm in its accounting and auditing practice,⁵ ~~which that~~ provides the firm with reasonable assurance that

Commented [CB2]: Revised to match the wording in SQMS 1

¹ Paragraph 35f of Statement on Quality Management Standards (SQMS) (previously Statement on Quality Control Standards) No. 1, *A Firm's System of Quality Management*.

² See footnote 1.

³ Paragraph 25 of SQMS No. 1.

⁴ Paragraph 35f of SQMS No. 1.

⁵ The term *auditing and accounting practice* is defined in paragraph 17a of SQMS No. 1.

- a. the firm and its personnel fulfill their responsibilities in accordance with professional standards and applicable legal and regulatory requirements, and conduct engagements in accordance with such standards and requirements; and
 - b. engagement reports issued by the firm or engagement partners are appropriate in the circumstances.⁶
7. As explained in SQMS No. 1, the public interest is served by the consistent performance of quality engagements. Quality engagements are achieved through planning and performing engagements and reporting on them in accordance with professional standards and applicable legal and regulatory requirements. Achieving the objectives of those standards and complying with the requirements of applicable law or regulation involves exercising professional judgment and, when applicable to the type of engagement, maintaining professional skepticism.
8. An engagement quality review is an objective evaluation of the significant judgments made by the engagement team and the conclusions reached thereon. The engagement quality reviewer's evaluation of significant judgments is performed in the context of professional standards and applicable legal and regulatory requirements. However, an engagement quality review is not intended to be an evaluation of whether the entire engagement complies with professional standards and applicable legal and regulatory requirements or with the firm's policies or procedures.
9. The engagement quality reviewer is not a member of the engagement team. The performance of an engagement quality review does not change the responsibilities of the engagement partner for managing and achieving quality on the engagement or for the direction and supervision of the members of the engagement team and the review of their work. The engagement quality reviewer is not required to obtain evidence to support the opinion or conclusion on the engagement, but the engagement team may obtain further evidence in responding to matters raised during the engagement quality review.

Authority of This SQMS

10. This SQMS contains the objective for the firm in following this SQMS and requirements designed to enable the firm and the engagement quality reviewer to meet that stated objective. In addition, it contains related guidance in the form of application and other explanatory material and introductory material that provides context relevant to a proper understanding of this SQMS and definitions. SQMS No. 1⁷ explains the terms *objective*, *requirements*, *application material and other explanatory material*, *introductory material*, and *definitions*.

Effective Date

11. This SQMS is effective for

⁶ Paragraph 15 of SQMS No. 1.

⁷ Paragraphs 12 and A6–A9 of SQMS No. 1.

- a. audits or reviews of financial statements for periods beginning on or after December 15, 2025, and
- b. other engagements in the firm’s accounting and auditing practice beginning on or after December 15, 2025.

Objective

12. The objective of the firm, through appointing an eligible engagement quality reviewer, is to perform an objective evaluation of the significant judgments made by the engagement team and the conclusions reached thereon.

Definitions

13. For purposes of the SQMSs, the following terms have the meanings attributed as follows:

Engagement quality review. An objective evaluation of the significant judgments made by the engagement team, and the conclusions reached thereon, performed by the engagement quality reviewer and completed before the engagement report is released.

Engagement quality reviewer. A partner, other individual in the firm, or an external individual appointed by the firm to perform the engagement quality review.

Relevant ethical requirements. Principles of professional ethics and ethical requirements to which the engagement team and engagement quality reviewer, when undertaking an engagement quality review, are subject, which consist of the AICPA Code of Professional Conduct together with rules of applicable state boards of accountancy and applicable regulatory agencies that are more restrictive. (Ref: par. A11–A14)

Requirements

Applying, and Complying With, Relevant Requirements

14. The firm and the engagement quality reviewer should have an understanding of this SQMS, including the application and other explanatory material, to understand the objective of this SQMS and to properly apply the requirements relevant to them.
15. The firm or the engagement quality reviewer, as applicable, should comply with each requirement of this SQMS, unless the requirement is not relevant in the circumstances of the engagement.
16. The proper application of the requirements is expected to provide a sufficient basis for the achievement of the objective of this standard. However, if the firm or the engagement quality reviewer determines that the application of the relevant requirements does not provide a sufficient basis for the achievement of the objective of this standard, the firm or the engagement quality reviewer, as applicable, should take further actions to achieve the objective.

Appointment and Eligibility of Engagement Quality Reviewers

17. The firm should establish policies or procedures that require the assignment of responsibility for the appointment of engagement quality reviewers to an individual or individuals with the competence, capabilities, and appropriate authority within the firm to fulfill the responsibility. Those policies or procedures should require such individual or individuals to appoint the engagement quality reviewer. (Ref: par. A1–A3)
18. The firm should establish policies or procedures that set forth the criteria for eligibility to be appointed as an engagement quality reviewer. Those policies or procedures should require that the engagement quality reviewer ~~not be a member of the engagement team and~~ (Ref: par. A4)
 - a. ~~has~~ **not be a member of the engagement team;**
 - b. ~~have~~ the competence and capabilities, including sufficient time, and the appropriate authority to perform the engagement quality review; (Ref: par. A5–A10)
 - c. ~~complies~~ **comply** with relevant ethical requirements, including those addressing threats to the objectivity and independence of the engagement quality reviewer; and (Ref: par. A11–~~A14~~**A13**)
 - d. ~~complies~~ **comply** with provisions of law and regulation, if any, that are relevant to the eligibility of the engagement quality reviewer. (Ref: par. ~~A15~~**A14**)
19. The firm's policies or procedures established in accordance with paragraph ~~18b~~**18c** should also address threats to objectivity created by an individual being appointed as the engagement quality reviewer after previously serving as the engagement partner. (Ref: par. ~~A16~~**A15**–A17)
20. The firm should establish policies or procedures that set forth the criteria for eligibility of individuals who assist the engagement quality reviewer. Those policies or procedures should require that such individuals
 - a. **not be members of the engagement team** and
 - b. have the competence and capabilities, including sufficient time, to perform the duties assigned to them, and (Ref: par. A18)
 - c. comply with relevant ethical requirements, including addressing threats to their objectivity and independence and, if applicable, the provisions of law and regulation. (Ref: par. A19–A20)
21. The firm should establish policies or procedures that
 - a. require the engagement quality reviewer to take overall responsibility for the performance of the engagement quality review; and
 - b. address the engagement quality reviewer's responsibility for determining the nature, timing, and extent of the direction and supervision of individuals assisting in the engagement quality review and the review of their work. (Ref: par. A21)

Commented [CB3]: Revised so all the criteria are treated consistently as part of the list

Commented [CB4]: If the changes to the preceding paragraph are accepted, this reference will need to be updated

Commented [CB5]: Since this is one of the criteria, should it be moved into the vertical list, as I've done in paragraph 18?

Impairment of the Engagement Quality Reviewer’s Eligibility to Perform the Engagement Quality Review

22. The firm should establish policies or procedures that address circumstances in which the engagement quality reviewer’s eligibility to perform the engagement quality review is impaired and the appropriate actions to be taken by the firm, including the process for identifying and appointing a replacement in such circumstances. (Ref: par. A22)
23. When the engagement quality reviewer becomes aware of circumstances that impair the engagement quality reviewer’s eligibility, the engagement quality reviewer should notify the appropriate individual or individuals in the firm and (Ref: par. A23)
 - a. if the engagement quality review has not commenced, decline the appointment to perform the engagement quality review, or
 - b. if the engagement quality review has commenced, discontinue the performance of the engagement quality review.

Performance of the Engagement Quality Review

24. The firm should establish policies or procedures regarding the performance of the engagement quality review that address the following:
 - a. The engagement quality reviewer’s responsibilities to perform procedures in accordance with paragraphs 25–26 at appropriate points in time during the engagement to provide an appropriate basis for an objective evaluation of the significant judgments made by the engagement team and the conclusions reached thereon
 - b. The responsibilities of the engagement partner in relation to the engagement quality review, including that the engagement partner is precluded from releasing the engagement report until notification has been received from the engagement quality reviewer, in accordance with paragraph 27, that the engagement quality review is complete (Ref: par. A24–~~A25~~A26)
 - c. Circumstances when in which the nature and extent of engagement team discussions with the engagement quality reviewer about a significant judgment give rise to a threat to the objectivity of the engagement quality reviewer and appropriate actions to take in these circumstances (Ref: par. ~~A26~~A27)
25. In performing the engagement quality review, the engagement quality reviewer should do the following: (Ref: par. ~~A27–A32~~A28–A33)
 - a. Read, and obtain an understanding about, information communicated by (Ref: par. ~~A33~~A34)
 - i. the engagement team regarding the nature and circumstances of the engagement and the entity; and
 - ii. the firm related to the firm’s monitoring and remediation process, in particular, identified deficiencies that may relate to, or affect, the areas involving significant judgments made by the engagement team.

Commented [AG6]: AICPA style

- b. Discuss with the engagement partner and, if applicable, other members of the engagement team, significant matters and significant judgments made in planning, performing, and reporting on the engagement. (Ref: par. ~~A34~~~~A37~~~~A35~~~~A38~~)
 - c. Based on the information obtained in (a) and (b), review selected engagement documentation relating to significant judgments made by the engagement team and evaluate the following: (Ref: par. ~~A38~~~~A42~~~~A39~~~~A43~~)
 - i. The basis for making those significant judgments, including, when applicable to the type of engagement, the maintenance of professional skepticism by the engagement team
 - ii. Whether the engagement documentation supports the conclusions reached
 - iii. Whether the conclusions reached are appropriate
 - d. Evaluate the basis for the engagement partner’s determination that relevant ethical requirements relating to independence, when applicable, have been fulfilled. (Ref: par. ~~A43~~~~A44~~)
 - e. Evaluate whether appropriate consultation has taken place on difficult or contentious matters or matters involving differences of opinion and the conclusions arising from those consultations. (Ref: par. ~~A44~~~~A45~~)
 - f. For engagements conducted in accordance with generally accepted auditing standards, evaluate the basis for the engagement partner’s determination that the engagement partner’s involvement has been sufficient and appropriate throughout the ~~audit~~ engagement such that the engagement partner has ~~the~~an appropriate basis for determining that the significant judgments made and the conclusions reached are appropriate given the nature and circumstances of the engagement. (Ref: par. ~~A45~~~~A46~~~~A47~~)
 - g. Review,
 - i. for audits of financial statements, the financial statements and the auditor’s report thereon, including, if applicable, the description of the key audit matters; (Ref: par. ~~A47~~~~A48~~)
 - ii. for reviews of financial statements or financial information, the financial statements or financial information and the review report thereon; or (Ref: par. ~~A47~~~~A48~~)
 - iii. for other engagements, the engagement report, and when applicable, the subject matter information. (Ref: par. ~~A48~~~~A49~~)
26. The engagement quality reviewer should notify the engagement partner if the engagement quality reviewer has concerns that the significant judgments made by the engagement team, including the appropriate maintenance of professional skepticism by the engagement team when applicable to the type of engagement, or the conclusions reached thereon, are not appropriate. If such concerns are not resolved to the engagement quality reviewer’s satisfaction, the engagement quality reviewer should notify the appropriate individual or

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Commented [CB8]: Should there be a modifier before “basis” here, like “an appropriate basis”? Or correct as is?

Commented [AG9R8]: This is how it is in the IAASB standards and also in the QM SAS, par. 40a (first bullet, which should be changed to lettered list). Change suggested in both places.

individuals in the firm that the engagement quality review cannot be completed. (Ref: par. ~~A49~~A50)

Completion of the Engagement Quality Review

27. The engagement quality reviewer should determine whether the requirements in this SQMS with respect to the performance of the engagement quality review have been fulfilled and whether the engagement quality review is complete. If so, the engagement quality reviewer should notify the engagement partner that the engagement quality review is complete.

Documentation

28. The firm should establish policies or procedures that require the engagement quality reviewer to take responsibility for documentation of the engagement quality review. (Ref: par. ~~A50~~A51)
29. The firm should establish policies or procedures that require documentation of the engagement quality review in accordance with paragraph 30 and require that such documentation be included with the engagement documentation.
30. The engagement quality reviewer should determine that the documentation of the engagement quality review is sufficient to enable an experienced practitioner, having no previous connection with the engagement, to understand the nature, timing, and extent of the procedures performed by the engagement quality reviewer and, when applicable, individuals who assisted the reviewer; and to understand the conclusions reached in performing the review. The engagement quality reviewer ~~also~~ should also determine that the documentation of the engagement quality review includes the following: (Ref: par. ~~A51–A53~~A52–A54)
- a. The names of the engagement quality reviewer and any individuals who assisted with the engagement quality review
 - b. An identification of the engagement documentation reviewed
 - c. The basis for the engagement quality reviewer’s determination in accordance with paragraph 27
 - d. The notifications required in accordance with paragraphs 26 and 27
 - e. The date of completion of the engagement quality review

Commented [AG10]: Editorial suggestions

Application and Other Explanatory Material

Appointment and Eligibility of Engagement Quality Reviewers

Assignment of Responsibility for the Appointment of Engagement Quality Reviewers (Ref: par. 17)

- A1. Competence and capabilities that are relevant to an individual’s ability to fulfill responsibility for the appointment of the engagement quality reviewer may include appropriate knowledge about the following:

- The responsibilities of an engagement quality reviewer
 - The criteria in paragraphs 18–19 regarding the eligibility of engagement quality reviewers
 - The nature and circumstances of the engagement or the entity subject to an engagement quality review, including the composition of the engagement team
- A2. The firm’s policies or procedures may specify that the individual responsible for the appointment of engagement quality reviewers not be a member of the engagement team for which an engagement quality review is to be performed. However, in certain circumstances (for example, in the case of a smaller firm or a sole practitioner), it may not be practicable for an individual other than a member of the engagement team to appoint the engagement quality reviewer.
- A3. The firm may assign more than one individual to be responsible for appointing engagement quality reviewers. For example, the firm’s policies or procedures may specify a different process for appointing engagement quality reviewers for audits of financial statements than for attestation examination engagements or other engagements, with different individuals responsible for each process.

Eligibility of the Engagement Quality Reviewer (Ref: par. 18)

- A4. In some circumstances, for example, in the case of a smaller firm or a sole practitioner, there may not be a partner or other individual in the firm who is eligible to perform the engagement quality review. In these circumstances, the firm may contract with, or obtain the services of, individuals external to the firm to perform the engagement quality review. An individual external to the firm may be a partner or an employee of a network firm, a structure or organization within the firm’s network, or a service provider. When using such an individual, the provisions in SQMS No. 1 addressing network requirements or network services or service providers apply.

Eligibility Criteria for the Engagement Quality Reviewer

Competence and Capabilities, Including Sufficient Time (Ref: par. 18a)

- A5. SQMS No. 1 describes characteristics related to competence, including the integration and application of technical competence, professional skills, and professional ethics, values, and attitudes.⁸ **Matters Characteristics** that the firm may consider in determining that an individual has the necessary competence to perform an engagement quality review include, for example, the following:
- An understanding of professional standards and applicable legal and regulatory requirements and the firm’s policies or procedures relevant to the engagement
 - Knowledge of the entity’s industry
 - An understanding of, and experience relevant to, engagements of a similar nature and complexity

Commented [AG11]: Editorial suggestion to clarify that the bullets apply to the individual, not the firm.

⁸ Paragraph A92 of SQMS No. 1.

- An understanding of the responsibilities of the engagement quality reviewer in performing and documenting the engagement quality review, which may be attained or enhanced by receiving relevant training from the firm

A6. The conditions, events, circumstances, actions, or inactions considered by the firm in determining that an engagement quality review is an appropriate response to address one or more quality risks⁹ may be ~~an important consideration into~~ the firm's determination of the competence and capabilities required to perform the engagement quality review for that engagement. Other considerations that the firm may take into account in determining whether the engagement quality reviewer has the competence and capabilities, including sufficient time, needed to evaluate the significant judgments made by the engagement team and the conclusions reached thereon include, for example, the following:

Commented [AG12]: To avoid using "consider" and "consideration" in the same sentence.

- The nature of the entity
- The specialization and complexity of the industry or regulatory environment in which the entity operates
- The extent to which the engagement relates to matters requiring specialized expertise (for example, with respect to IT or specialized areas of accounting or auditing), or scientific and engineering expertise, which may be needed for certain assurance engagements (Also see paragraph A19.)

A7. In evaluating the competence and capabilities of an individual who may be appointed as an engagement quality reviewer, the findings arising from the firm's monitoring activities (for example, findings from the inspection of engagements for which the individual was an engagement team member or engagement quality reviewer) or the results of external inspections may also be relevant considerations.

A8. A lack of appropriate competence or capabilities affects the ability of the engagement quality reviewer to exercise appropriate professional judgment in performing the review. For example, an engagement quality reviewer who lacks relevant industry experience may not possess the ability or confidence necessary to evaluate and, when appropriate, challenge significant judgments made and the maintenance of professional skepticism by the engagement team on a complex, industry-specific accounting or auditing matter.

Appropriate Authority (Ref: par. 18a)

A9. Actions at the firm level help to establish the authority of the engagement quality reviewer. For example, ~~by creating when the firm has created~~ a culture of respect for the role of the engagement quality reviewer, the engagement quality reviewer is less likely to experience pressure from the engagement partner or other personnel to inappropriately influence the outcome of the engagement quality review. In some cases, the engagement quality reviewer's authority may be enhanced by the firm's policies or procedures to address differences of opinion, which may include actions the engagement quality reviewer may take when a disagreement occurs between the engagement quality reviewer and the engagement team.

Commented [CB13]: Right now, this reads as saying that the engagement quality reviewer is the one creating a culture of respect for the role of the engagement quality reviewer. Is that correct?
If not, considering revising to something like "...by creating a culture of respect for the role of the engagement quality reviewer, the firm makes it less likely that the engagement quality reviewer will experience pressure..."

Commented [AG14R13]: Good catch!

⁹ See footnote 8.

A10. The authority of the engagement quality reviewer may be diminished when

- the culture within the firm promotes respect for authority only for personnel at a higher level of hierarchy within the firm.
- the engagement quality reviewer has a reporting line to the engagement partner, for example, when the engagement partner holds a leadership position in the firm or is responsible for determining the compensation of the engagement quality reviewer.

Relevant Ethical Requirements (Ref: par. 13c and 18b)

A11. The relevant ethical requirements that are applicable when undertaking an engagement quality review may vary, depending on the nature and circumstances of the engagement or the entity. Various provisions of relevant ethical requirements may apply to an individual, such as an engagement quality reviewer, and not the firm itself. For example, if a firm uses an external provider to perform an engagement quality review, that individual may be subject to independence requirements; however, the independence requirements imposed on that individual as a result of performing the engagement quality review may not extend to the entire firm for which that individual works.

~~Relevant ethical requirements may also include provisions that address threats to independence created by long association with an audit or assurance client. The application of any such provisions dealing with long association is distinct from, but may need to be taken into consideration in applying, the required cooling-off period in accordance with paragraph 19.~~

Commented [AG15]: As directed by the ASB in January – see par. A13

Threats to the Objectivity of the Engagement Quality Reviewer

A12. Threats to the engagement quality reviewer’s objectivity may be created by a broad range of facts and circumstances. Examples follow:

- A self-review threat may be created when the engagement quality reviewer previously was involved with significant judgments made by the engagement team, in particular, as the engagement partner or ~~other~~another engagement team member.
- A familiarity or self-interest threat may arise when the engagement quality reviewer is a close or immediate family member of the engagement partner or another member of the engagement team, or through close personal relationships with members of the engagement team.
- An intimidation threat may be created when actual or perceived pressure is exerted on the engagement quality reviewer (for example, when the engagement partner is an aggressive or dominant individual, or the engagement quality reviewer has a reporting line to the engagement partner).

Commented [CB16]: Can we use “another” here? or correct as is?

A13. Relevant ethical requirements may include requirements and guidance to identify, evaluate, and address threats to objectivity. ~~They may also include provisions that address threats to independence created by long association with an audit or assurance client.~~

Commented [AG17]: As directed by the ASB in January – see deleted par. A11

Law or Regulation Relevant to the Eligibility of the Engagement Quality Reviewer (Ref: par 18c)

A14. Law or regulation may prescribe additional requirements regarding the eligibility of the engagement quality reviewer. For example, the audit requirements of the FDIC regulations for certain financial institutions require the auditor (which includes the engagement quality reviewer) to be in compliance with the AICPA's Code of Professional Conduct and also meet the independence requirements and interpretations of the SEC and its staff.

Commented [CB18]: Okay to assume readers don't need this spelled out on first mention?

~~*Cooling-Off Period for an Individual After Previously Serving as Considerations Related to Assigning the Previous Engagement Partner as Engagement Quality Reviewer (Ref: par. 19)*~~

Commented [AG19]: As directed by the ASB

A15. In recurring engagements, the matters on which significant judgments are made often do not vary. Therefore, significant judgments made in prior periods may continue to affect judgments of the engagement team in subsequent periods. Therefore, the ability of an engagement quality reviewer to perform an objective evaluation of significant judgments is affected when the individual was previously involved with those judgments as the engagement partner. In such circumstances, it is important that appropriate safeguards are put in place to reduce threats to objectivity, in particular, the self-review threat, to an acceptable level. ~~Accordingly, this proposed SQMS requires the firm to establish policies or procedures that specify a cooling-off period during which the engagement partner is precluded from being appointed as the engagement quality reviewer.~~ The following factors may be taken into consideration when designing policies and procedures to maintain the objectivity of an engagement quality reviewer who served as the engagement partner on the previous year's engagement:

- The extent of changes in the matters on which significant judgments are made and the facts and circumstances around those significant judgments compared to the period(s) or periods in which the individual was the engagement partner. For example, if a ~~new accounting pronouncement has been implemented~~ business combination with a material effect on the financial statements or key management personnel changes have occurred, the significant judgments made in the current period may vary from those of the prior period to such an extent that an objective evaluation of those judgments could be made by the individual who served as the engagement partner in the previous period.
- The procedures and incentives placed by the firm's system of quality management on objective reviews (for example, ~~the engagement quality reviewer would not be penalized for identifying a misstatement related to a year in which the reviewer was the engagement partner~~) whether the firm has a culture of accountability that focuses on improving identified deficiencies or a culture of blame that focuses on penalizing people).

~~**A16.**~~ **A16AA** A firm may establish policies or procedures that limit the eligibility of individuals to be appointed as engagement quality reviewers of individuals who previously served as the engagement partner, for example, by establishing a specified cooling-off period during which the engagement partner is precluded from being appointed as the engagement quality reviewer.

Determining a suitable cooling-off period depends ~~upon~~ the facts and circumstances of the engagement.

Commented [AG20]: As directed by ASB

Commented [AG21]: Editorial

A17. The firm's policies or procedures ~~may~~ also ~~may~~ address whether a cooling-off period is appropriate for an individual other than the engagement partner before becoming eligible to be appointed as the engagement quality reviewer on that engagement. In this regard, the firm may consider the nature of that individual's role and previous involvement with the significant judgments made on the engagement. For example, the firm may determine that an engagement partner responsible for the performance of audit procedures on the financial information of a component in a group audit engagement may not be eligible to be appointed as the group engagement quality reviewer because of that audit partner's involvement in the significant judgments affecting the group audit engagement.

Circumstances in Which the Engagement Quality Reviewer Uses Assistants (Ref: par. 20–21)

A18. In certain circumstances, it may be appropriate for the engagement quality reviewer to be assisted by an individual or team of individuals. For example, assistance from individuals with highly specialized knowledge, skills, or expertise may be useful for understanding certain transactions undertaken by the entity to help the engagement quality reviewer evaluate the significant judgments made by the engagement team related to those transactions.

A19. The guidance in paragraph A14 may be helpful to the firm when establishing policies or procedures that address threats to objectivity of individuals who assist the engagement quality reviewer.

A20. When the engagement quality reviewer is assisted by an individual external to the firm, the assistant's responsibilities, including those related to compliance with relevant ethical requirements, may be set out in the contract or other agreement between the firm and the assistant.

A21. The firm's policies or procedures may include responsibilities of the engagement quality reviewer to

- consider whether assistants understand their instructions and whether the work is being carried out in accordance with the planned approach to the engagement quality review and
- address matters raised by assistants, considering their significance and modifying the planned approach appropriately.

Impairment of the Engagement Quality Reviewer's Eligibility to Perform the Engagement Quality Review (Ref: par. 22–23)

A22. Factors that may be relevant to the firm in considering whether the eligibility of the engagement quality reviewer to perform the engagement quality review is impaired include the following:

- Whether changes in the circumstances of the engagement result in the engagement quality reviewer no longer having the appropriate competence and capabilities to perform the review
- Whether changes in the other responsibilities of the engagement quality reviewer indicate that the individual no longer has sufficient time to perform the review

- Notification from the engagement quality reviewer in accordance with paragraph 23

A23. In circumstances in which the engagement quality reviewer's eligibility to perform the engagement quality review becomes impaired, the firm's policies or procedures may set out a process by which alternative eligible individuals are identified. The firm's policies or procedures may also address the responsibility of the individual appointed to replace the engagement quality reviewer to perform procedures sufficient to fulfill the requirements of this SQMS with respect to the performance of the engagement quality review. Such policies or procedures may further address the need for consultation in such circumstances and may include, for example, the following:

- Evaluation of whether procedures performed by the previous engagement quality reviewer could be relied ~~upon~~ by the newly assigned engagement quality reviewer or whether all work would need to be reperformed
- Consideration of the effect of an engagement quality review assistant on the transition, when such assistant has been involved in the engagement quality review prior to transition
- Procedures undertaken by the engagement team to inform the newly assigned engagement quality reviewer about planning meeting discussions that have already occurred and other matters in which the previous engagement quality reviewer had been involved
- Documentation of the circumstances necessitating the change

Performance of the Engagement Quality Review (Ref: par. 24–27)

Engagement Partner Responsibilities in Relation to the Engagement Quality Review (Ref: par. 24b)

A24. Statement on Auditing Standards (SAS) No. 146, *Quality Management for an Engagement Conducted in Accordance With Generally Accepted Auditing Standards*,¹⁰ establishes the requirements for the engagement partner in audit engagements for which an engagement quality review is required, including the following:

- ~~determining~~Determining that an engagement quality reviewer has been appointed;
- ~~cooperating~~Cooperating with the engagement quality reviewer and informing other members of the engagement team of their responsibility to do so;
- ~~discussing~~Discussing significant matters and significant judgments arising during the audit engagement, including those identified during the engagement quality review, with the engagement quality reviewer; ~~and~~
- ~~not~~Not releasing the auditor's report until the completion of the engagement quality review.

Commented [CB22]: Revised because, per style, this list is too long and complex to ideally be treated as a grammatical continuation of the lead-in sentence

¹⁰ Paragraph 36 of Statement on Auditing Standards (SAS) No. 146, *Quality Management for an Engagement Conducted in Accordance With Generally Accepted Auditing Standards*.

~~A25.A24A.~~ Professional standards require that the engagement report not be dated earlier than the date on which sufficient appropriate engagement evidence has been obtained. If the engagement quality review is completed after the report is dated and identifies instances where additional procedures are needed or additional in which the report was dated before sufficient appropriate engagement evidence is required has been obtained, the date of the report is required to be changed to the date when the additional procedures have been satisfactorily completed or the additional evidence has been obtained, in accordance with the professional standards applicable to the engagement. Such instances, if not rare, may be indicative of a deficiency or deficiencies in the firm's system of quality management.

Commented [AG23]: As directed by the ASB.

A26. AT-C section 105, *Concepts Common to All Attestation Engagements*,^{11,*} also establishes requirements for the engagement partner in relation to the engagement quality review.

Discussions Between the Engagement Quality Reviewer and the Engagement Team (Ref: par. 24c)

A27. Frequent communication between the engagement team and engagement quality reviewer throughout the engagement may assist in facilitating an effective and timely engagement quality review. However, a threat to the objectivity of the engagement quality reviewer may be created depending on the timing and extent of the discussions with the engagement team about a significant judgment. The firm's policies or procedures may set out the actions to be taken by the engagement quality reviewer or the engagement team to avoid situations in which the engagement quality reviewer is, or may be perceived to be, making decisions on behalf of the engagement team. For example, in these circumstances, the firm may require consultation about such significant judgments with other relevant personnel in accordance with the firm's consultation policies or procedures.

Procedures Performed by the Engagement Quality Reviewer (Ref: par. 25–27)

A28. The firm's policies or procedures may specify the nature, timing, and extent of the procedures performed by the engagement quality reviewer and also may emphasize the importance of the engagement quality reviewer exercising professional judgment in performing the review.

A29. The timing of the procedures performed by the engagement quality reviewer may depend on the nature and circumstances of the engagement or the entity, including the nature of the matters subject to the review. Timely review of the engagement documentation by the engagement quality reviewer throughout all stages of the engagement (for example, planning, performing, and reporting) allows matters to be promptly resolved to the engagement quality reviewer's satisfaction before the release of the engagement report. For example, the engagement quality reviewer may perform procedures in relation to the overall strategy and plan for the engagement at the completion of the planning phase. Timely performance of the engagement quality review may also reinforce the exercise of professional judgment and, when

¹¹ Paragraph 36 of International Standard on Assurance Engagements (ISAE) 3000 (Revised), *Assurance Engagements Other than Audits or Reviews of Historical Financial Information*.

* All AT-C sections can be found in AICPA *Professional Standards*.

applicable to the type of engagement, maintenance of professional skepticism, by the engagement team in planning and performing the engagement.

A30. The nature and extent of the engagement quality reviewer's procedures for a specific engagement may depend on the following, among other factors:

- The reasons for the assessments given to quality risks,¹² for example, engagements performed for entities in emerging industries or with complex transactions.
- Identified deficiencies, and the remedial actions to address the identified deficiencies, related to the firm's monitoring and remediation process, and any related guidance issued by the firm, which may indicate areas where more extensive procedures need to be performed by the engagement quality reviewer.
- The complexity of the engagement.
- The nature and size of the entity, including whether the entity is a listed entity.
- Findings relevant to the engagement, such as the results of inspections undertaken by an external oversight authority in a prior period, or other concerns raised about the quality of the work of the engagement team.
- Information obtained from the firm's acceptance and continuance of client relationships and specific engagements.
- For assurance engagements, the engagement team's identification and assessment of, and responses to, risks of material misstatement in the engagement.
- Whether members of the engagement team have cooperated with the engagement quality reviewer. The firm's policies or procedures may address the actions the engagement quality reviewer takes in circumstances **whenin which** the engagement team has not cooperated with the engagement quality reviewer, for example, informing an appropriate individual in the firm so appropriate action can be taken to resolve the issue.

Commented [AG24]: AICPA style

A31. The nature, timing, and extent of the engagement quality reviewer's procedures may need to change based on circumstances encountered in performing the engagement quality review.

Group Audit Considerations

A32. The performance of an engagement quality review for an audit of group financial statements may involve additional considerations for the individual appointed as the engagement quality reviewer for the group audit, depending on the size and complexity of the group. Paragraph 21a requires the firm's policies or procedures to require the engagement quality reviewer to take overall responsibility for the performance of the engagement quality review. In doing so, for larger and more complex group audits, the group engagement quality reviewer may need to discuss significant matters and significant judgments with key members of the engagement team other than the group engagement team (for example, those responsible for performing

¹² Paragraph A49 of SQMS No. 1.

audit procedures on the financial information of a component). In these circumstances, the engagement quality reviewer may be assisted by individuals in accordance with paragraph 20. The guidance in paragraph A22 may be helpful when the engagement quality reviewer for the group audit is using assistants.

- A33.** In some cases, an engagement quality reviewer may be appointed for an audit of an entity or business unit that is part of a group, for example, when such an audit is required by law, regulation, or for other reasons. In these circumstances, communication between the engagement quality reviewer for the group audit and the engagement quality reviewer for the audit of that entity or business unit may help the group engagement quality reviewer in fulfilling the responsibilities in accordance with paragraph 21a. For example, this may be the case when the entity or business unit has been identified as a component for purposes of the group audit and significant judgments related to the group audit have been made at the component level.

Information Communicated by the Engagement Team and the Firm (Ref: par. 25a)

- A34.** Obtaining an understanding of information communicated by the engagement team and the firm in accordance with paragraph 25a may assist the engagement quality reviewer in understanding the significant judgments that may be expected for the engagement. Such an understanding may also provide the engagement quality reviewer with a basis for discussions with the engagement team about the significant matters and significant judgments made in planning, performing, and reporting on the engagement. For example, a deficiency identified by the firm may relate to significant judgments made by other engagement teams for certain accounting estimates for a particular industry. When this is the case, such information may be relevant to the significant judgments made on the engagement with respect to those accounting estimates and, therefore, may provide the engagement quality reviewer with a basis for discussions with the engagement team in accordance with paragraph 25b.

Significant Matters and Significant Judgments (Ref: par. 25b–c)

- A35.** For audits of financial statements, SAS No. 146¹³ requires the engagement partner to review audit documentation relating to significant matters¹⁴ and significant judgments, including those relating to difficult or contentious matters identified during the engagement, and the conclusions reached.
- A36.** For audits of financial statements, SAS No. 146¹⁵ provides examples of significant judgments that may be identified by the engagement partner related to the overall audit strategy and audit plan for undertaking the engagement, the execution of the engagement, and the overall conclusions reached by the engagement team.
- A37.** For engagements other than audits of financial statements, the significant judgments made by the engagement team may depend on the nature and circumstances of the engagement or the entity. For example, in an attestation engagement performed in accordance with

¹³ Paragraph 31 of SAS No. 146.

¹⁴ Paragraph .08c of AU-C section 230, *Audit Documentation*. All AU-C sections can be found in AICPA *Professional Standards*.

¹⁵ Paragraph A93 of SAS No. 146.

Statements on Standards for Attestation Engagements, the engagement team's determination of whether the criteria to be applied in the preparation of the subject matter information are suitable for the engagement may involve or require significant judgment.

- A38.** In performing the engagement quality review, the engagement quality reviewer may become aware of other areas where significant judgments would have been expected to be made by the engagement team for which further information may be needed about the engagement team's procedures performed or the basis for conclusions reached. In those circumstances, discussions with the engagement quality reviewer may result in the engagement team concluding that additional procedures need to be performed.
- A39.** The information obtained in accordance with paragraphs 25a–b, and the review of selected documentation, assists the engagement quality reviewer in evaluating the engagement team's basis for making the significant judgments. Other considerations that may be relevant to the engagement quality reviewer's evaluation include, for example, the following:
- Remaining alert to changes in the nature and circumstances of the engagement or the entity that may result in changes in the significant judgments made by the engagement team
 - Applying an unbiased view in evaluating responses from the engagement team
 - Following up on inconsistencies identified in reviewing engagement documentation or inconsistent responses by the engagement team to questions relating to the significant judgments made
- A40.** The firm's policies or procedures may specify engagement documentation to be reviewed by the engagement quality reviewer. In addition, such policies or procedures may indicate that the engagement quality reviewer exercises professional judgment in selecting additional engagement documentation to be reviewed relating to significant judgments made by the engagement team.
- A41.** Discussions about significant judgments with the engagement partner and, if applicable, other members of the engagement team, together with the engagement team's documentation, may assist the engagement quality reviewer in evaluating the maintenance of professional skepticism, when applicable to the engagement, by the engagement team in relation to those significant judgments.
- A42.** For audits of financial statements, SAS No. 146¹⁶ provides examples of the impediments to the maintenance of professional skepticism at the engagement level, unconscious auditor biases that may impede the maintenance of professional skepticism, and possible actions that the engagement team may take to mitigate impediments to the maintenance of professional skepticism at the engagement level.
- A43.** For audits of financial statements, the requirements and relevant application material in ~~proposed SASAU-C section 315~~, *Understanding the Entity and Its Environment and*

¹⁶ Paragraphs A33–A35 of SAS No. 146.

Assessing the Risks of Material Misstatement;¹⁷ AU-C section 540, *Auditing Accounting Estimates and Related Disclosures*;¹⁸ and other AU-C sections also provide examples of areas in an audit where the auditor maintains professional skepticism or examples of where appropriate documentation may help provide evidence about how the auditor maintained professional skepticism. Such guidance may also assist the engagement quality reviewer in evaluating the maintenance of professional skepticism by the engagement team.

Whether Relevant Ethical Requirements Relating to Independence Have Been Fulfilled (Ref: par. 25d)

A44. SAS No. 146¹⁹ requires the engagement partner, prior to dating the auditor's report, to take responsibility for determining whether relevant ethical requirements, including those related to independence, have been fulfilled.

Whether Consultation Has Taken Place on Difficult or Contentious Matters or Matters Involving Differences of Opinion (Ref: par. 25e)

A45. SQMS No. 1²⁰ addresses consultation on difficult or contentious matters and differences of opinion within the engagement team, or between the engagement team and the engagement quality reviewer or individuals performing activities within the firm's system of quality management.

Sufficient and Appropriate Involvement of the Engagement Partner on the Engagement (Ref: par. 25f)

A46. SAS No. 146²¹ requires the engagement partner to determine, prior to dating the auditor's report, that the engagement partner's involvement has been sufficient and appropriate throughout the audit engagement such that the engagement partner has the basis for determining that the significant judgments made and the conclusions reached are appropriate given the nature and circumstances of the engagement. SAS No. 146²² also indicates that the documentation of the involvement of the engagement partner may be accomplished in different ways. Discussions with the engagement team, and review of such engagement documentation, may assist the engagement quality reviewer's evaluation of the basis for the engagement partner's determination that the engagement partner's involvement has been sufficient and appropriate.

A47. SAS No. 146 is adapted, as necessary, to engagements performed in accordance with generally accepted auditing standards other than audits of financial statements. Accordingly, the requirement in paragraph 25f is applicable to those engagements.

Engagement Quality Reviewer's Review of Financial Statements and Engagement Reports (Ref:

¹⁷ Paragraph A255 of AU-C section 315, *Understanding the Entity and Its Environment and Assessing the Risks of Material Misstatement*.

¹⁸ Paragraph .A11 of AU-C section 540, *Auditing Accounting Estimates and Related Disclosures*.

¹⁹ Paragraph 21 of SAS No. 146.

²⁰ Paragraphs 32d–e and A80–A83 of SQMS No. 1.

²¹ Paragraph 40a of SAS No. 146.

par. 25g)

- A48.** For audits of financial statements, the engagement quality reviewer's review of the financial statements and auditor's report thereon is consistent with the engagement quality reviewer's understanding of those matters based on the review of selected engagement documentation and discussions with the engagement team. In reviewing the financial statements, the engagement quality reviewer may also become aware of other areas where significant judgments would have been expected to be made by the engagement team for which further information may be needed about the engagement team's procedures or conclusions. The guidance in this paragraph also applies to reviews of financial statements and the related engagement report.
- A49.** For engagements other than audits or reviews of financial statements, the engagement quality reviewer's review of the engagement report and, when applicable, the subject matter information may include considerations similar to those described in paragraph [A45A46](#) (for example, whether the presentation or description of matters relating to the significant judgments made by the engagement team are consistent with the engagement quality reviewer's understanding based on the procedures performed in connection with the engagement quality review).

Unresolved Concerns of the Engagement Quality Reviewer (Ref: par. 26)

- A50.** The firm's policies or procedures may specify the individual or individuals in the firm to be notified if the engagement quality reviewer has unresolved concerns that the significant judgments made by the engagement team, or the conclusions reached thereon, are not appropriate. Such individuals may include the individual assigned the responsibility for the appointment of engagement quality reviewers. With respect to such unresolved concerns, the firm's policies or procedures may also require consultation within or outside the firm (for example, a professional or regulatory body).

Documentation (Ref: par. 28–30)

- A51.** Paragraphs 58–61 of SQMS No. 1 address the firm's documentation of its system of quality management, which includes the firm's policies and procedures addressing engagements that are required to be subject to engagement quality reviews. This SQMS addresses additional documentation requirements related to such policies and procedures as well as documentation requirements related to the performance of engagement quality reviews undertaken at the engagement level.
- A52.** The form, content, and extent of the documentation of the engagement quality review may depend on the following factors:
- The nature and complexity of the engagement
 - The nature of the entity
 - The nature and complexity of the matters subject to the engagement quality review
 - The extent of the engagement documentation reviewed

- A53.** The performance and notification of the completion of the engagement quality review may be documented in a number of ways. For example, the engagement quality reviewer may document the review of engagement documentation electronically in the IT application for the performance of the engagement. Alternatively, the engagement quality reviewer may document the review through means of a memorandum. The engagement quality reviewer's procedures may also be documented in other ways, for example, in the minutes of the engagement team's discussions when the engagement quality reviewer was present.
- A54.** Paragraph 24*b* requires that the firm's policies or procedures preclude the engagement partner from releasing the engagement report until the completion of the engagement quality review, which includes resolving matters raised by the engagement quality reviewer. Provided that all requirements with respect to the performance of the engagement quality review have been fulfilled, the documentation of the review may be finalized after the release of the engagement report but before the assembly of the final engagement file.

Proposed



ASB Meeting
May 11-12, 2022
Agenda Item 2C

Statement on Auditing Standards *Quality Management for an Engagement Conducted in Accordance With Generally Accepted Auditing Standards*

Commented [AG1]: Note: For ease of reading and to speed the turnaround and issuance of the final standard, the word "proposed" has been added as a watermark, deleted from the text and not shown in track changes; and references have been updated to refer to SQMS Nos. 1 and 2.

Proposed

CONTENTS

	Paragraph
Introduction	
Scope of this SAS	1
The Firm's System of Quality Management and Role of Engagement Teams	2-9
Effective Date	10
Objective	11
Definitions	12
Requirements	
Leadership Responsibilities for Managing and Achieving Quality on Audits	13-15
Relevant Ethical Requirements, Including Those Related to Independence	16-21
Acceptance and Continuance of Client Relationships and Audit Engagements	22-24
Engagement Resources	25-28
Engagement Performance	29-38
Monitoring and Remediation	39
Taking Overall Responsibility for Managing and Achieving Quality	40
Documentation	41
Application and Other Explanatory Material	
Scope of this SAS	A1
The Firm's System of Quality Management and Role of Engagement Teams	A2-A14
Definitions	A15-A27
Leadership Responsibilities for Managing and Achieving Quality on Audits	A28-A37
Relevant Ethical Requirements, Including Those Related to Independence	A38-A48
Acceptance and Continuance of Client Relationships and Audit Engagements	A49-A58

Agenda Item 2C – QM marked from January ASB meeting

Engagement Resources	A59–A80
Engagement Performance	A81–A109
Monitoring and Remediation	A110–A113
Taking Overall Responsibility for Managing and Achieving Quality	A114–A117
Documentation	A118–A121

Proposed

Statement on Auditing Standards *Quality Management for an Engagement Conducted in Accordance With Generally Accepted Auditing Standards*

Introduction

Scope of This Statement on Auditing Standards

1. This Statement on Auditing Standards (SAS) addresses the specific responsibilities of the auditor regarding quality management at the engagement level for an audit of financial statements and the related responsibilities of the engagement partner. This SAS also applies, adapted as necessary, to other engagements conducted in accordance with generally accepted auditing standards (GAAS) (for example, a review of interim financial information conducted in accordance with AU-C section 930, *Interim Financial Information*).^{*} This SAS is to be read in conjunction with the AICPA Code of Professional Conduct (AICPA code) and other relevant ethical requirements. (Ref: par. A1 and A38)
2. Although government audit organizations are subject to the quality control and assurance requirements of *Government Auditing Standards*, and Statements on Quality Management Standards (SQMSs) are not applicable to auditors in government audit organizations,¹ this SAS is applicable to auditors in government audit organizations who perform financial audits in accordance with GAAS.

The Firm's System of Quality Management and the Role of Engagement Teams

3. Under SQMS No. 1, *A Firm's System of Quality Management*, the objective of the firm is to design, implement, and operate a system of quality management for engagements performed by the firm in its accounting and auditing practice that provides the firm with reasonable assurance that (Ref: par. A2–A3)
 - a. the firm and its personnel fulfill their responsibilities in accordance with professional standards and applicable legal and regulatory requirements and conduct engagements in accordance with such standards and requirements, and
 - b. engagement reports issued by the firm or engagement partners are appropriate in the circumstances.²
4. The engagement team, led by the engagement partner, is responsible, within the context of the firm's system of quality management and through complying with the requirements of this SAS, for the following: (Ref: par. A4–A11)
 - a. Implementing the firm's responses to quality risks (that is, the firm's policies or procedures) that are applicable to the audit engagement using information communicated by, or obtained from, the firm
 - b. Given the nature and circumstances of the audit engagement, determining whether to design and implement responses at the engagement level beyond those in the firm's policies or procedures

Commented [AG2]: Note: For ease of reading and to speed the turnaround and issuance of the final standard, the word "proposed" has been added as a watermark, deleted from the text and not shown in track changes; and references have been updated to refer to SQMS Nos. 1 and 2.

^{*} All AU-C sections can be found in AICPA *Professional Standards*.

¹ Paragraph 5 of Statement on Quality Management Standards (SQMS) No. 1, *A Firm's System of Quality Management*.

² Paragraph 15 of SQMS No. 1.

- c. Communicating to the firm information from the audit engagement that is required ~~to be communicated~~ by the firm's policies or procedures to ~~be communicated to~~ support the design, implementation, and operation of the firm's system of quality management.

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5. Complying with the requirements in other AU-C sections may provide information that is relevant to quality management at the engagement level. (Ref: par. A12)

6. The public interest is served by the consistent performance of quality audit engagements, ~~which are engagements that achieve through achieving~~ the objective of this SAS and other AU-C sections ~~for each engagement~~. A quality audit engagement is achieved through planning and performing the engagement and reporting on it in accordance with professional standards and applicable legal and regulatory requirements. Achieving the objectives of those standards and complying with the requirements of applicable law or regulation involves exercising professional judgment and maintaining professional skepticism.

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7. In accordance with AU-C section 200, *Overall Objectives of the Independent Auditor and the Conduct of an Audit in Accordance With Generally Accepted Auditing Standards*,³ the engagement team is required to plan and perform an audit with professional skepticism and to exercise professional judgment. Professional judgment is exercised in making informed decisions about the courses of action that are appropriate to manage and achieve quality given the nature and circumstances of the audit engagement. Professional skepticism supports the quality of judgments made by the engagement team and, through these judgments, supports the overall effectiveness of the engagement team in achieving quality at the engagement level. The appropriate maintenance of professional skepticism may be demonstrated through the actions and communications of the engagement team. Such actions and communications may include specific steps to mitigate impediments that may impair the appropriate maintenance of professional skepticism, such as unconscious bias or resource constraints. (Ref: par. A33–A36)

Scalability

8. The requirements of this SAS are intended to be applied in the context of the nature and circumstances of each audit. Examples follow:

- When an audit is carried out entirely by the engagement partner, which may be the case for an audit of a less complex entity, some requirements in this SAS are not relevant because they are conditional on the involvement of other members of the engagement team. (Ref: par. A13–A14)
- When an audit is not carried out entirely by the engagement partner, or in an audit of an entity whose nature and circumstances are more complex, the engagement partner may assign the design or performance of some procedures, tasks, or actions to other members of the engagement team.

The Engagement Partner's Responsibilities

9. The engagement partner remains ultimately responsible and, therefore, accountable, for compliance with the requirements of this SAS. ~~Nevertheless, the engagement partner may seek assistance from others to fulfill these responsibilities.~~ The phrase "take responsibility for..." is used for those

³ Paragraphs .17–.18 and .A22–.A31 of AU-C section 200, *Overall Objectives of the Independent Auditor and the Conduct of an Audit in Accordance With Generally Accepted Auditing Standards*.

requirements for which the engagement partner is permitted to assign the design or performance of procedures, tasks, or actions to appropriately skilled or suitably experienced members of the engagement team. For other requirements, this SAS expressly intends that the requirement or responsibility be fulfilled by the engagement partner, ~~and~~. In such circumstances, the engagement partner may need to obtain information from the firm or other members of the engagement team. For example, when others perform supervisory and review responsibilities, the outcome of those activities can be taken into account by the engagement partner in fulfilling the requirement. (Ref: par. A22–A25)

Commented [AG5]: In response to ASB discussion in January.

Effective Date

10. This SAS is effective for engagements conducted in accordance with GAAS for periods beginning on or after December 15, 2025.

Objective

11. The objective of the auditor is to manage quality at the engagement level to obtain reasonable assurance that quality has been achieved such that

- a. the auditor has fulfilled the auditor's responsibilities, and has conducted the audit, in accordance with professional standards and applicable legal and regulatory requirements, and
- b. the auditor's report issued is appropriate in the circumstances.

Definitions

12. For purposes of GAAS, the following terms have the meanings attributed as follows:

Engagement partner.⁴ The partner or other individual appointed by the firm who is responsible for the audit engagement and its performance, and for the auditor's report that is issued on behalf of the firm, and who, when required, has the appropriate authority from a professional, legal, or regulatory body.

Engagement quality review. An objective evaluation of the significant judgments made by the engagement team and the conclusions reached thereon, performed by the engagement quality reviewer and completed before the engagement report is released.

Engagement quality reviewer. A partner, other individual in the firm, or an external individual appointed by the firm to perform the engagement quality review.

Engagement team. All partners and staff performing the audit engagement and any other individuals who perform audit procedures on the engagement, excluding an auditor's external specialist⁵ and internal auditors who provide direct assistance on an engagement.⁶ (Ref: par. A15–A25)

Firm. A form of organization permitted by law or regulation whose characteristics conform to resolutions of the Council of the AICPA and that is engaged in public practice. (Ref: par. A26)

Commented [AG6]: To conform with extant

Inspection. Inspection is a retrospective evaluation of the adequacy of aspects of the firm's quality management policies and procedures, its personnel's understanding of those policies and procedures, and the extent of the firm's compliance with them.

Commented [AG7]: As discussed in January

Commented [AG8]: To be consistent with SQMS 1

⁴ *Engagement partner, partner, and firm* refer to their governmental equivalents when relevant.

⁵ Paragraph .06 of AU-C section 620, *Using the Work of an Auditor's Specialist*, defines the term *auditor's specialist*.

⁶ AU-C section 610, *Using the Work of Internal Auditors*, establishes limits on the use of direct assistance.

Network. ~~As defined in "Definitions" (ET sec. 0.400)† in the AICPA code, an~~ association of entities that includes one or more firms, ~~as defined in "Definitions" (ET section 0.400) in the AICPA code~~ (Ref: par. A27)

Commented [AG9]: To clarify

Network firm. ~~A firm or other entity that belongs to a network, as~~ defined in "Definitions" (ET section ~~sec. 0.400~~) in the AICPA code, ~~a firm or other entity that belongs to a network.~~ References to a *network firm* are to be read hereafter as "another firm or entity that belongs to the same network as the firm." (Ref: par. A27)

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Partner. Any individual with authority to bind the firm with respect to the performance of a professional services engagement. For purposes of this definition, *partner* may include an employee with this authority who has not assumed the risks and benefits of ownership. Firms might use different titles to refer to individuals with this authority.

Personnel. Partners and staff in the firm.

Professional standards. Standards promulgated by the AICPA Auditing Standards Board or the AICPA Accounting and Review Services Committee under the "General Standards Rule" (ET sec. 1.300.001) or the "Compliance With Standards Rule" (ET sec. 1.310.001) of the AICPA code, or by other standard-setting bodies that set auditing and attest standards applicable to the engagement being performed and relevant ethical requirements.

Relevant ethical requirements. Principles of professional ethics and ethical requirements to which the engagement team and engagement quality reviewer are subject, which consist of the AICPA code together with rules of applicable state boards of accountancy and applicable regulatory agencies that are more restrictive.

Response (in relation to a system of quality management). Policies or procedures designed and implemented by the firm to address one or more quality risks:

- Policies are statements of what should, or should not, be done to address a quality risk or risks. Such statements may be documented, explicitly stated in communications, or implied through actions and decisions.
- Procedures are actions to implement policies.

Staff. Professionals, other than partners, including any specialist the firm employs.

Requirements

Leadership Responsibilities for Managing and Achieving Quality on Audits

13. The engagement partner should take overall responsibility for managing and achieving quality on the audit engagement, including taking responsibility for creating an environment for the engagement that emphasizes the firm's culture and expected behavior of engagement team members. In doing so, the engagement partner should be sufficiently and appropriately involved throughout the audit engagement such that the engagement partner has the basis for determining whether the significant judgments made, and the conclusions reached, are appropriate given the nature and circumstances of the engagement. (Ref: par. A28–A37)

14. In creating the environment described in paragraph 13, the engagement partner should take responsibility for clear, consistent, and effective actions being taken that reflect the firm's commitment to quality and that establish and communicate the expected behavior of engagement team members, including emphasizing the following: (Ref: par. A30–A34)

† All ET sections can be found in AICPA *Professional Standards*.

- a. That all engagement team members are responsible for contributing to the management and achievement of quality at the engagement level
- b. The importance of professional ethics, values, and attitudes to the members of the engagement team
- c. The importance of open and robust communication within the engagement team and supporting the ability of engagement team members to raise concerns without fear of reprisal
- d. The importance of each engagement team member maintaining professional skepticism throughout the audit engagement

15. If the engagement partner assigns the design or performance of procedures, tasks, or actions related to a requirement of this SAS to other members of the engagement team to assist the engagement partner in complying with the requirements of this SAS, the engagement partner should continue to take overall responsibility for managing and achieving quality on the audit engagement through direction and supervision of those members of the engagement team and review of their work. (Ref: par. 9 and A37)

Relevant Ethical Requirements, Including Those Related to Independence

16. The engagement partner should have an understanding of the relevant ethical requirements, including those related to independence, that are applicable given the nature and circumstances of the audit engagement. (Ref: par. A38–A42 and A48)

17. The engagement partner should take responsibility for other members of the engagement team having been made aware of relevant ethical requirements that are applicable given the nature and circumstances of the audit engagement, and the firm's related policies or procedures, including those that address the following: (Ref: par. A23–A25 and A40–A44)

- a. Identifying, evaluating, and addressing threats to compliance with relevant ethical requirements, including those related to independence
- b. Circumstances that may cause a breach of relevant ethical requirements, including those related to independence, and the responsibilities of members of the engagement team when they become aware of breaches
- c. The responsibilities of members of the engagement team when they become aware of an instance of noncompliance with laws and regulations by the entity⁷

18. If matters come to the engagement partner's attention that indicate that a threat to compliance with relevant ethical requirements exists, the engagement partner should evaluate the threats by complying with the firm's policies or procedures, using relevant information from the firm, the engagement team, or other sources, and take appropriate action. (Ref: par. A43–A44)

19. The engagement partner should remain alert throughout the audit engagement, through observation and making inquiries as necessary, for breaches of relevant ethical requirements or the firm's related policies or procedures by members of the engagement team. (Ref: par. A45)

20. If matters come to the engagement partner's attention through the firm's system of quality management, or from other sources, that indicate that relevant ethical requirements applicable to the nature

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⁷ See AU-C section 250, *Consideration of Laws and Regulations in an Audit of Financial Statements*.

and circumstances of the audit engagement have not been fulfilled, the engagement partner, in consultation with others in the firm, should take appropriate action. (Ref: par. A46)

21. Prior to dating the auditor's report, the engagement partner should take responsibility for determining whether relevant ethical requirements, including those related to independence, have been fulfilled. (Ref: par. A38 and A47)

Acceptance and Continuance of Client Relationships and Audit Engagements

22. The engagement partner should determine that the firm's policies or procedures for the acceptance and continuance of client relationships and audit engagements have been followed, and that conclusions reached in this regard are appropriate. (Ref: par. A49–A52, A58)

23. The engagement partner should take into account information obtained in the acceptance and continuance process in planning and performing the audit engagement in accordance with GAAS and complying with the requirements of this SAS. (Ref: par. A53–A56)

24. If the engagement team becomes aware of information that may have caused the firm to decline the audit engagement had that information been known by the firm prior to accepting or continuing the client relationship or specific engagement, the engagement partner should communicate that information promptly to the firm so that the firm and the engagement partner can take the necessary action. (Ref: par. A57)

Engagement Resources

25. The engagement partner should determine that sufficient and appropriate resources to perform the engagement are assigned or made available to the engagement team in a timely manner, taking into account the nature and circumstances of the audit engagement, the firm's policies or procedures, and any changes that may arise during the engagement. (Ref: par. A59–~~A70A~~, ~~A73–A71~~, ~~A74~~, ~~A75~~, and ~~A79A80~~)

26. The engagement partner should determine that members of the engagement team, and any auditor's external specialists and internal auditors who provide direct assistance who are not part of the engagement team, collectively have the appropriate competence and capabilities, including sufficient time, to perform the audit engagement. (Ref: par. A62 and ~~A71–A74A72–A75~~)

27. If, as a result of complying with the requirements in paragraphs 25 and 26, the engagement partner determines that resources assigned or made available are insufficient or inappropriate in the circumstances of the audit engagement, the engagement partner should take appropriate action, including communicating with appropriate individuals about the need to assign or make available additional or alternative resources to the engagement. (Ref: par. ~~A75–A78A76–A79~~)

28. The engagement partner should take responsibility for using the resources assigned or made available to the engagement team appropriately, given the nature and circumstances of the audit engagement. (Ref: par. A63–A69)

Engagement Performance

Direction, Supervision, and Review

29. The engagement partner should take responsibility for the direction and supervision of the members of the engagement team and the review of their work. (Ref: par. ~~A80A81~~)

30. The engagement partner should determine that the nature, timing, and extent of direction, supervision, and review ~~is~~are (Ref: par. ~~A81–A89~~A82–A90 and ~~A94–A97~~A95–A98)
- planned⁸ and performed in accordance with the firm's policies or procedures, professional standards, and applicable legal and regulatory requirements, and
 - responsive to the nature and circumstances of the audit engagement and the resources assigned or made available to the engagement team by the firm.
31. The engagement partner should review audit documentation at appropriate points in time during the audit engagement, including audit documentation relating to (Ref: par. ~~A90–A93~~A91–A94)
- significant matters;⁹
 - significant judgments, including those relating to difficult or contentious matters identified during the audit engagement, and the conclusions reached; and
 - other matters that, in the engagement partner's professional judgment, are relevant to the engagement partner's responsibilities.
32. On or before the date of the auditor's report, the engagement partner should determine, through review of audit documentation and discussion with the engagement team, that sufficient appropriate audit evidence has been obtained to support the conclusions reached and for the auditor's report to be issued. (Ref: par. ~~A90–A94~~A91–A95)
33. Prior to dating the auditor's report, the engagement partner should review the financial statements and the auditor's report, including, if applicable, the description of the key audit matters¹⁰ and related audit documentation, to determine that the report to be issued will be appropriate in the circumstances.¹¹
34. The engagement partner should review, prior to their issuance, formal written communications to management, those charged with governance, or regulatory authorities. (Ref: par. ~~A98~~A99)

Consultation

35. The engagement partner should ~~do the following~~ (Ref: par. ~~A99–A102~~A100–A103)
- ~~take~~Take responsibility for the engagement team undertaking consultation on
 - difficult or contentious matters and matters on which the firm's policies or procedures require consultation;⁷ and
 - other matters that, in the engagement partner's professional judgment, require consultation;²
 - ~~determine~~Determine that members of the engagement team have undertaken appropriate consultation during the audit engagement, both within the engagement team⁷ and between the engagement team and others at the appropriate level within or outside the firm;²

Commented [AG12]: Editorial, because otherwise the sentence is too long.

⁸ Paragraph .11 of AU-C section 300, *Planning an Audit of Financial Statements*.

⁹ Paragraph .08 of AU-C section 230, *Audit Documentation*.

¹⁰ See AU-C section 701, *Communicating Key Audit Matters in the Auditor's Report*.

¹¹ See AU-C section 700, *Forming an Opinion and Reporting on Financial Statements*, or AU-C section 705, *Modifications to the Opinion in the Independent Auditor's Report*.

- c. ~~determine~~Determine that the nature and scope of, and conclusions resulting from, such consultations are agreed with the party consulted, ~~and~~.
- d. ~~determine~~Determine that conclusions agreed have been implemented.

Engagement Quality Review

36. For audit engagements for which an engagement quality review is required, the engagement partner should (Ref: par. ~~A103~~A104)
- a. determine that an engagement quality reviewer has been appointed.
 - b. cooperate with the engagement quality reviewer and inform other members of the engagement team of their responsibility to do so.
 - c. discuss significant matters and significant judgments arising during the audit engagement, including those identified during the engagement quality review, with the engagement quality reviewer, ~~and~~.
 - d. not release the auditor's report until the completion of the engagement quality review. (Ref: par. ~~A104–A106~~A105–A107)

Differences of Opinion

37. If differences of opinion arise within the engagement team, or between the engagement team and the engagement quality reviewer or individuals performing activities within the firm's system of quality management, including those who provide consultation, the engagement team should follow the firm's policies or procedures for dealing with and resolving such differences of opinion. (Ref: par. ~~A107–A108–A109~~)
38. The engagement partner should
- a. take responsibility for differences of opinion being addressed and resolved in accordance with the firm's policies or procedures.
 - b. determine that conclusions reached are documented and implemented, ~~and~~.
 - c. not date the auditor's report until any differences of opinion are resolved.

Monitoring and Remediation

39. The engagement partner should take responsibility for the following: (Ref: par. ~~A109–A112~~A110–A113)
- a. Obtaining an understanding of the information from the firm's monitoring and remediation process, as communicated by the firm, including, as applicable, the information from the monitoring and remediation process of the network and across the network firms
 - b. Determining the relevance and effect on the audit engagement of the information referred to in paragraph 39a and ~~take~~taking appropriate action
 - c. Remaining alert throughout the audit engagement for information that may be relevant to the firm's monitoring and remediation process and ~~communicate~~communicating such information to those responsible for the process

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Taking Overall Responsibility for Managing and Achieving Quality

40. Prior to dating the auditor's report, the engagement partner should determine that the engagement partner has taken overall responsibility for managing and achieving quality on the audit engagement. In doing so, the engagement partner should determine that (Ref: par. ~~A113–A116~~~~A114–A117~~)

- a. the engagement partner's involvement has been sufficient and appropriate throughout the audit engagement such that the engagement partner has ~~the an appropriate~~ basis for determining that the significant judgments made and the conclusions reached are appropriate given the nature and circumstances of the engagement; ~~and,~~
- b. the nature and circumstances of the audit engagement, any changes thereto, and the firm's related policies or procedures have been taken into account in complying with the requirements of this ~~proposed~~-SAS.

Commented [AG15]: Suggestion from Editorial

Documentation

41. In applying AU-C section 230, *Audit Documentation*, the auditor should include the following in the audit documentation:¹² (Ref: par. ~~A117–A120~~~~A118–A121~~)

- a. Significant issues identified, relevant discussions with personnel, and conclusions reached with respect to
 - i. fulfillment of responsibilities relating to relevant ethical requirements, including those related to independence
 - ii. the acceptance and continuance of the client relationship and audit engagement
- b. The nature and scope of, and conclusions resulting from, consultations undertaken during the audit engagement and how such conclusions were implemented
- c. If the audit engagement is subject to an engagement quality review, that the engagement quality review has been completed before the release of the auditor's report

Application and Other Explanatory Material

Scope of This ~~Proposed~~ SAS (Ref: par. 1)

A1. This SAS applies to all audits of financial statements, including audits of group financial statements. AU-C section 600, *Special Considerations — Audits of Group Financial Statements (Including the Work of Component Auditors)*, deals with special considerations that apply to an audit of group financial statements, including when component auditors are involved. AU-C section 600 also provides guidance on how to adapt and apply the requirements of this SAS in an audit of group financial statements involving component auditors. AU-C section 600, adapted as necessary in the circumstances, may also be useful in an audit of financial statements when the engagement team includes individuals from another firm. For example, AU-C section 600 may be useful when involving such an individual to attend a physical inventory count; inspect property, plant, and equipment; or perform audit procedures at a shared service center at a remote location.

The Firm's System of Quality Management and ~~the~~ Role of Engagement Teams (Ref: par. 3–9)

A2. SQMS No. 1 addresses a firm's responsibilities for designing, implementing, and operating its system of quality management.

¹² Paragraphs .08–.11 of AU-C section 230.

A3. Firms may use different terminology or frameworks to describe the components of the system of quality management.

The Engagement Team’s Responsibilities Relating to the Firm’s System of Quality Management (Ref: par. 4)

A4. Quality management at the engagement level is supported by the firm’s system of quality management and informed by the specific nature and circumstances of the audit engagement. In accordance with SQMS No. 1, the firm is responsible for communicating information that enables the engagement team to understand and carry out their responsibilities relating to performing engagements. For example, such communications may cover policies or procedures to undertake consultations with designated individuals in certain situations involving complex technical or ethical matters or to involve firm-designated experts in specific engagements to perform audit procedures related to particular matters (for example, the firm may specify that firm-designated credit-risk modeling experts are to be involved in auditing expected credit loss allowances in audits of financial institutions).

A5. Firm-level responses may include policies or procedures established by a network or by other firms, structures, or organizations within the same network (network requirements or network services are described further in SQMS No. 1 within the “Network Requirements or Network Services” section).¹³ The requirements of this SAS are based on the premise that the firm is responsible for taking the necessary action to enable engagement teams to implement or use network requirements or network services on the audit engagement (for example, a requirement to use an audit methodology developed for use by a network firm). Under SQMS No. 1, the firm is responsible for determining how network requirements or network services are relevant to, and are taken into account in, the firm’s system of quality management.¹⁴

A6. Some firm-level responses to quality risks are not performed at the engagement level but are, nevertheless, relevant when complying with the requirements of this SAS. For example, firm-level responses that the engagement team may be able to depend on when complying with the requirements of this SAS include the following:

- personnel ~~Personnel~~ recruitment and professional training processes,
- ~~the~~ The IT applications that support the firm’s monitoring of independence,
- ~~the~~ The development of IT applications that support the acceptance and continuance of client relationships and audit engagements, ~~and~~
- ~~the~~ The development of audit methodologies and related implementation tools and guidance.

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A7. Due to the specific nature and circumstances of each audit engagement and changes that may occur during the audit engagement, a firm cannot identify all quality risks that may arise at the engagement level or set forth all relevant and appropriate responses. Accordingly, the engagement team exercises professional judgment in determining whether to design and implement responses, beyond those set forth in the firm’s policies or procedures, at the engagement level to meet the objective of this SAS.¹⁵

A8. The engagement team’s determination of whether engagement-level responses are necessary (and, if so, what those responses are) is influenced by the requirements of this SAS, the engagement team’s

¹³ Paragraph 50b of SQMS No. 1.

¹⁴ Paragraph 50a of SQMS No. 1.

¹⁵ AU-C section 200 requires the auditor to exercise professional judgment in planning and performing an audit of financial statements.

understanding of the nature and circumstances of the engagement, and any changes during the audit engagement. For example, unanticipated circumstances may arise during the engagement that may cause the engagement partner to request the involvement of appropriately experienced personnel in addition to those initially assigned or made available by the firm.

A9. The relative balance of the engagement team's efforts to comply with the requirements of this SAS (that is, between implementing the firm's responses and designing and implementing engagement-specific responses beyond those set forth in the firm's policies or procedures) may vary. For example, the firm may design an audit program to be used in circumstances that are applicable to the audit engagement (for example, an industry-specific audit program). Other than determining the timing and extent of procedures to be performed, there may be little or no need for supplemental audit procedures to be added to the audit program at the engagement level. Alternatively, the engagement team's actions in complying with the engagement performance requirements of this SAS may be more focused on designing and implementing responses at the engagement level to deal with the specific nature and circumstances of the engagement (for example, planning and performing procedures to address risks of material misstatement not contemplated by the firm's audit programs).

A10. Ordinarily, the engagement team may depend on the firm's policies or procedures in complying with the requirements of this SAS, unless

- the engagement team's understanding or practical experience indicates that the firm's policies or procedures will not effectively address the nature and circumstances of the engagement, or
- information provided by the firm or other parties, about the effectiveness of such policies or procedures suggests otherwise they cannot be relied on (for example, information provided by the firm's monitoring activities, external inspections, or other relevant sources indicates that the firm's policies or procedures are not operating effectively).

Commented [AG17]: Editorial suggestion for clarity

A11. If the engagement partner becomes aware (including by being informed by other members of the engagement team) that the firm's responses to quality risks are ineffective in the context of the specific engagement, or the engagement partner is unable to depend on the firm's policies or procedures, the engagement partner communicates such information promptly to the firm in accordance with paragraph 39c because such information is relevant to the firm's monitoring and remediation process. For example, if an engagement team member identifies that an audit software program has a security weakness, timely communication of such information to the appropriate personnel enables the firm to take steps to update and reissue the audit program. See also paragraph A69 in respect of sufficient and appropriate resources.

Information Relevant to Quality Management at the Engagement Level (Ref: par. 5)

A12. Complying with the requirements in other AU-C sections may provide information that is relevant to quality management at the engagement level. For example, the understanding of the entity and its environment required to be obtained under AU-C section 315, *Understanding the Entity and Its Environment and Assessing the Risks of Material Misstatement*, provides information that may be relevant to complying with the requirements of this SAS. Such information may be relevant to the determination of one or more of the following:

- The nature of resources to deploy for specific audit areas, such as the use of appropriately experienced team members for high-risk areas or the involvement of experts to deal with complex matters

- The amount of resources to allocate to specific audit areas, such as the number of team members assigned to attend the physical inventory count at multiple locations
- The nature, timing, and extent of review of the work performed by members of the team based on the assessed risks of material misstatement
- The allocation of the budgeted audit hours, including allocating more time and the time of more experienced engagement team members to those areas where there are more risks of material misstatement or the identified risks are assessed as higher

Scalability (Ref: par. 8)

A13. In a smaller firm, the firm's policies or procedures may designate an engagement partner or partners, on behalf of the firm, to design many of the responses to the firm's quality risks because doing so may be a more effective approach to designing and implementing responses as part of the firm's system of quality management. Additionally, a smaller firm's policies or procedures may be less formal. For example, in a very small firm with a relatively small number of audit engagements, the firm may determine that there is no need to establish a firm-wide system to monitor independence and, rather, independence will be monitored at the individual engagement level by the engagement partner.

A14. The requirements relating to direction, supervision, and review of the work of other members of the engagement team are only relevant if there are members of the engagement team other than the engagement partner.

Definitions

Engagement Team (Ref: par. 12)

A15. The engagement team may be organized in a variety of ways. For example, engagement team members may be located together or across different geographic locations and may be organized in groups by the activity they are performing. Regardless of how the engagement team is organized, any individual who performs audit procedures¹⁶ on the audit engagement, excluding an auditor's external specialist¹⁷ and internal auditors who provide direct assistance on an engagement,¹⁸ is a member of the engagement team.

A16. The definition of an *engagement team* focuses on individuals who perform audit procedures on the audit engagement. *Audit evidence*, which is necessary to support the auditor's opinion and report, is primarily obtained from audit procedures performed during the course of the audit.¹⁹ Audit procedures comprise risk assessment procedures²⁰ and further audit procedures.²¹ As explained in AU-C section 500, *Audit Evidence*, audit procedures include inspection, observation, confirmation, recalculation, reperformance, analytical procedures, and inquiry, often performed in some combination.²² Other AU-C

¹⁶ Paragraph .A44 of AU-C section 500, *Audit Evidence*.

¹⁷ Paragraph .06 of AU-C section 620 defines the term *auditor's specialist*.

¹⁸ AU-C section 610 establishes limits on the use of direct assistance.

¹⁹ Paragraph .A32 of AU-C section 200.

²⁰ AU-C section 315, *Understanding the Entity and Its Environment and Assessing the Risks of Material Misstatement*, provides requirements related to risk assessment procedures.

²¹ AU-C section 330, *Performing Audit Procedures in Response to Assessed Risks and Evaluating the Audit Evidence Obtained*, provides requirements related to further audit procedures, including tests of controls and substantive procedures.

²² Paragraph .A43 of AU-C section 500.

sections may also include specific procedures to obtain audit evidence, for example, AU-C section 520, *Analytical Procedures*.

A17. Engagement teams include personnel and may also include other individuals who perform audit procedures who are from

- a network firm, ~~or~~
- a firm that is not a network firm, or
- another service provider.²³

For example, an individual from another firm may perform audit procedures on the financial information of a component in a group audit engagement, attend a physical inventory count, or inspect physical fixed assets at a remote location.

A18. Engagement teams may also include individuals from service delivery centers who perform audit procedures. For example, it may be determined that specific tasks that are repetitive or specialized in nature will be performed by a group of appropriately skilled personnel; thus, the engagement team includes such individuals. Service delivery centers may be established by the firm, the network, or by other firms, structures, or organizations within the same network. For example, a centralized function may be used to facilitate external confirmation procedures.

A19. Engagement teams may include individuals with expertise in a specialized area of accounting or auditing who perform audit procedures on the audit engagement, for example, individuals with expertise in accounting for income taxes or in analyzing complex information produced by automated tools and techniques for the purpose of identifying unusual or unexpected relationships. An individual is not a member of the engagement team if that individual's involvement with the engagement is limited to consultation. Consultations are addressed in paragraphs 35 and A99–A102.

A20. If the audit engagement is subject to an engagement quality review, the engagement quality reviewer, and any other individuals performing the engagement quality review, are not members of the engagement team. Such individuals may be subject to specific independence requirements.

A21. An internal auditor providing direct assistance and an auditor's external specialist whose work is used in the engagement are not members of the engagement team.²⁴ AU-C section 610, *Using the Work of Internal Auditors*, and section 620, *Using the Work of an Auditor's Specialist*, provide requirements and guidance for the auditor when using the work of internal auditors in a direct assistance capacity or when using the work of an external specialist, respectively. Compliance with these AU-C sections requires the auditor to obtain sufficient appropriate audit evidence on the work performed by an internal auditor who is providing direct assistance and to perform audit procedures on the work of an auditor's specialist.

The Engagement Partner's Responsibilities (Ref: par. 9, 12)

A22. When this SAS expressly intends that a requirement or responsibility be fulfilled by the engagement partner, the engagement partner may need to obtain information from the firm or other members of the engagement team to fulfill the requirement (for example, information to make the required decision or judgment). For example, the engagement partner is required to determine that members of the engagement team collectively have the appropriate competence and capabilities to perform the audit engagement. To make a judgment on whether the competence and capabilities of the engagement team is/are appropriate, the engagement partner may need to use information compiled by the engagement team or from the firm's system of quality management.

The Application of Firm Policies or Procedures by Members of the Engagement Team (Ref: par. 8 and par. 17)

²³ Paragraph 17v of proposed SQMS No. 1.

²⁴ See paragraphs .12–.13 of AU-C section 620 and paragraphs .20–.24 of AU-C section 610.

Commented [AG18]: Note, the third bullet was moved from the end of the second bullet, at Editorial's suggestion, for clarity

Commented [AG19]: Because competence and capabilities are two attributes, not one.

A23. Within the context of the firm's system of quality management, engagement team members from the firm are responsible for implementing the firm's policies or procedures that are applicable to the audit engagement. Engagement team members from another firm are neither partners nor staff of the engagement partner's firm. As such, they may not be subject to the firm's system of quality management or the firm's policies or procedures. Further, the policies or procedures of another firm may not be similar to ~~that those~~ of the engagement partner's firm. For example, policies or procedures regarding direction, supervision, and review may be different, particularly when the other firm is in a jurisdiction with a different legal system, language, or culture than that of the engagement partner's firm. Accordingly, when the engagement team includes individuals who are from another firm, different actions may need to be taken by the firm or the engagement partner to implement the firm's policies or procedures with respect to the work of those individuals.

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A24. In particular, the firm's policies or procedures may require the firm or the engagement partner to take different actions from those applicable to personnel when obtaining an understanding of whether an individual from another firm

- has the appropriate competence and capabilities to perform the audit engagement. For example, the individual would not be subject to the firm's recruitment and training processes, and therefore, the firm's policies or procedures may state that this determination can be made through other actions such as obtaining information from the other firm or a licensing or oversight body. Paragraphs 22 and A47–A48 of AU-C section 600 contain guidance on obtaining an understanding of the competence and capabilities of component auditors.
- understands the ethical requirements that are relevant to the group audit engagement. For example, the individual would not be subject to the firm's training with regard to the firm's policies or procedures for relevant ethical requirements. The firm's policies or procedures may state that this understanding is obtained through other actions such as providing information, manuals, or guides containing the provisions of the relevant ethical requirements applicable to the audit engagement to the individual.
- will confirm independence. For example, individuals who are not personnel may not be able to complete independence declarations directly on the firm's independence systems. The firm's policies or procedures may state that such individuals can provide evidence of their independence in relation to the audit engagement in other ways, such as through written confirmation.

A25. When firm policies or procedures require specific activities to be undertaken in certain circumstances (for example, consultation on a particular matter), it may be necessary to communicate with individuals who are not personnel about what is expected of them to enable the engagement partner to comply with the firm's policies or procedures. For example, in a group audit engagement, communicating the group auditor's policies and procedures about matters subject to consultation to a component auditor enables the component auditor to determine which identified difficult or contentious matters that are relevant to the group financial statements to bring to the attention of the group engagement team.

Firm (Ref: par. 12)

A26. The definition of *firm* in relevant ethical requirements may differ from the definition set out in this SAS.

“Network” and “Network Firm” (Ref: par. 12)

A27. The definitions of *network* or *network firm* in relevant ethical requirements may differ from those set out in this SAS. The AICPA code also provides guidance in relation to the terms *network* and *network firm*. Networks and other network firms may be structured in a variety of ways and are in all cases external to the firm. The provisions in this SAS in relation to networks also apply to any structures or organizations that do not form part of the firm but that exist within the network.

Leadership Responsibilities for Managing and Achieving Quality in Audits (Ref: par. 13–15)

Taking Overall Responsibility for Managing and Achieving Quality

A28. SQMS No. 1 requires the firm to establish quality objectives that address the firm's governance and leadership ~~that supports, which support~~ the design, implementation, and operation of the system of quality management. The engagement partner's responsibility for managing and achieving quality is supported by a firm culture that demonstrates a commitment to quality. In addressing the requirements in paragraphs 13 and 14 of this SAS, the engagement partner may communicate directly to other members of the engagement team and reinforce this communication through personal conduct and actions ~~(for example, such as~~ leading by example). A culture that demonstrates a commitment to quality is further shaped and reinforced by the engagement team members as they demonstrate expected behaviors when performing the engagement.

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Scalability

A29. The nature and extent of the actions of the engagement partner to demonstrate the firm's commitment to quality may depend on a variety of factors, including the size, structure, geographical dispersion, and complexity of the firm and the engagement team and the nature and circumstances of the audit engagement. With a smaller engagement team with few engagement team members, influencing the desired culture through direct interaction and conduct may be sufficient, whereas for a larger engagement team that is dispersed over many locations, more formal communications may be necessary.

Sufficient and Appropriate Involvement

A30. Being sufficiently and appropriately involved throughout the audit engagement may be demonstrated by the engagement partner in different ways, including the following:

- Taking responsibility for the nature, timing, and extent of the direction and supervision of the members of the engagement team and the review of their work in complying with the requirements of this SAS
- Varying the nature, timing, and extent of such direction, supervision, and review in the context of the nature and circumstances of the engagement

Communication

A31. Communication is the means through which the engagement team shares relevant information on a timely basis to comply with the requirements of this SAS, thereby contributing to the achievement of quality on the audit engagement. Communication may be between or among members of the engagement team or with

- a. the firm; (for example, individuals performing activities within the firm's system of quality management, including those assigned ultimate or operational responsibility for the firm's system of quality management),
- b. others involved in the audit (for example, internal auditors who provide direct assistance²⁵ or an auditor's external specialist²⁶), ~~and/or~~
- c. parties that are external to the firm (for example, management, those charged with governance, or regulatory authorities).

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²⁵ See paragraph .A47 of AU-C section 610.

²⁶ See paragraphs .11c and .A33 of AU-C section 620.

A32. The nature and circumstances of the audit engagement may affect the engagement partner's decisions regarding the appropriate means of effective communication with the members of the engagement team. For example, to support appropriate direction, supervision, and review, the firm may use IT applications to facilitate the communication between the members of the engagement team when they are performing work across different geographical locations.

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Professional Skepticism (Ref: par. 7)

A33. The engagement partner is responsible for emphasizing the importance of each engagement team member maintaining professional skepticism throughout the audit engagement. Conditions inherent in some audit engagements can create pressures on the engagement team that may impede the appropriate exercise of professional skepticism when designing and performing audit procedures and evaluating audit evidence. Accordingly, when developing the overall audit strategy in accordance with AU-C section 300, *Planning an Audit*, the engagement team may need to consider whether such conditions exist in the audit engagement and, if so, what actions the firm or the engagement team may need to undertake to mitigate such impediments.

A34. Impediments to the exercise of professional skepticism at the engagement level may include the following:

- Budget constraints, which may discourage the use of sufficiently experienced or technically qualified resources, including experts, necessary for audits of entities in which technical expertise or specialized skills are needed for effective understanding, assessment of, and responses to risks and informed questioning of management.
- Tight deadlines, which may negatively affect the behavior of those who perform the work as well as those who direct, supervise, and review. For example, external time pressures may create restrictions to analyzing complex information effectively.
- Lack of cooperation or undue pressures imposed by management, which may negatively affect the engagement team's ability to resolve complex or contentious issues.
- Insufficient understanding of the entity and its environment, its system of internal control, and the applicable financial reporting framework, which may constrain the ability of the engagement team to make appropriate judgments and an informed questioning of management's assertions.
- Difficulties in obtaining access to records, facilities, certain employees, customers, vendors, or others, which may cause the engagement team to bias the selection of sources of audit evidence and seek audit evidence from sources that are more easily accessible.
- Overreliance on automated tools and techniques, which may result in the engagement team not critically assessing audit evidence.

A35. Unconscious or conscious auditor biases may affect the engagement team's professional judgments, including, for example, in the design and performance of audit procedures, or the evaluation of audit evidence. Examples of unconscious auditor biases that may impede the exercise of professional skepticism and, therefore, the reasonableness of the professional judgments made by the engagement team in complying with the requirements of this SAS may include the following:

- *Availability bias*, which is a tendency to place more weight on events or experiences that immediately come to mind or are readily available than on those that are not
- *Confirmation bias*, which is a tendency to place more weight on information that corroborates an existing belief than information that contradicts or casts doubt on that belief

- *Groupthink*, which is a tendency to think or make decisions as a group ~~that discourages~~ **discouraging** creativity or individual responsibility
- *Overconfidence bias*, which is a tendency to overestimate one's own ability to make accurate assessments of risk or other judgments or decisions
- *Anchoring bias*, which is a tendency to use an initial piece of information as an anchor against which subsequent information is inadequately assessed
- *Automation bias*, which is a tendency to favor output generated from automated systems, even when human reasoning or contradictory information raises questions about whether such output is reliable or fit for purpose

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A36. Possible actions that the engagement team may take to mitigate impediments to the exercise of professional skepticism at the engagement level may include the following:

- Remaining alert to changes in the nature or circumstances of the audit engagement that necessitate additional or different resources for the engagement and requesting additional or different resources from those individuals within the firm responsible for allocating or assigning resources to the engagement
- Explicitly alerting the engagement team to instances or situations in which vulnerability to unconscious or conscious auditor biases may be greater (for example, areas involving greater judgment) and emphasizing the importance of seeking advice from more experienced members of the engagement team in planning and performing audit procedures
- Changing the composition of the engagement team, for example, requesting that more experienced individuals with greater skills or knowledge or specific expertise ~~are be~~ assigned to the engagement
- Involving more experienced members of the engagement team when dealing with members of management who are difficult or challenging to interact with
- Involving members of the engagement team with specialized skills and knowledge or an auditor's expert to assist the engagement team with complex or subjective areas of the audit
- Modifying the nature, timing, and extent of direction, supervision, or review by involving more experienced engagement team members, more in-person oversight on a more frequent basis, or more in-depth reviews of certain working papers for
 - complex or subjective areas of the audit,
 - areas that pose risks to achieving quality on the audit engagement,
 - areas with a fraud risk, and
 - identified or suspected noncompliance with laws or regulations
- Setting expectations for
 - less experienced members of the engagement team to seek advice frequently and in a timely manner from more experienced engagement team members or the engagement partner, and

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- more experienced members of the engagement team to be available to less experienced members of the engagement team throughout the audit engagement and to respond positively and in a timely manner to their insights, requests for advice, or assistance
- Communicating with those charged with governance when management imposes undue pressure or the engagement team experiences difficulties in obtaining access to records, facilities, certain employees, customers, vendors, or others from whom audit evidence may be sought

Assigning Procedures, Tasks, or Actions to Other Members of the Engagement Team (Ref: par. 15)

A37. Being sufficiently and appropriately involved throughout the audit engagement when procedures, tasks, or actions have been assigned to other members of the engagement team may be demonstrated by the engagement partner in different ways, including the following:

- Informing assignees about the nature of their responsibilities and authority, the scope of the work being assigned and the objectives thereof, and ~~to provide any other necessary instructions and relevant information~~
- ~~Direction~~ **Directing** and ~~supervision of~~ **supervising** the assignees
- ~~Review of~~ **Reviewing** the assignees' work to evaluate the conclusions reached, in addition to the requirements in paragraphs 29–34

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Relevant Ethical Requirements, Including Those Related to Independence (Ref: par. 16–21)

Relevant Ethical Requirements (Ref: par. 1, 16–21)

A38. AU-C section 200²⁷ requires that the auditor comply with relevant ethical requirements, ~~including those pertaining to independence,~~ relating to financial statement audit engagements, ~~including those requirements pertaining to independence.~~ Relevant ethical requirements may vary depending on the nature and circumstances of the engagement. For example, certain requirements related to independence may be applicable only when performing audits of depository institutions or employee benefit plans. AU-C section 600 includes additional requirements and guidance to those in this SAS regarding communications about relevant ethical requirements with component auditors.

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A39. Based on the nature and circumstances of the audit engagement, certain law, regulation, or aspects of relevant ethical requirements, such as those pertaining to noncompliance with laws or regulations, may be relevant to the engagement (for example, laws or regulations dealing with money laundering, corruption, or bribery).

A40. The firm's information system and the resources provided by the firm may assist the engagement team in understanding and fulfilling relevant ethical requirements applicable to the nature and circumstances of the audit engagement. For example, the firm may do the following:

- Communicate the independence requirements to engagement teams.
- Provide training for engagement teams on relevant ethical requirements.
- Establish manuals and guides (that is, intellectual resources) containing the provisions of the relevant ethical requirements and guidance on how they are applied in the nature and circumstances of the firm and its engagements.

²⁷ Paragraphs .16 and .A15–.A21 of AU-C section 200.

- Assign personnel to manage and monitor compliance with relevant ethical requirements (for example, SQMS No. 1 requires that the firm obtains, at least annually, a documented confirmation of compliance with the independence requirements from all personnel required by relevant ethical requirements to be independent) or provide consultation on matters related to relevant ethical requirements.
- Establish policies or procedures for engagement team members to communicate relevant and reliable information to appropriate parties within the firm or to the engagement partner, such as policies or procedures for engagement teams to
 - communicate information about client engagements and the scope of services, including nonassurance services, to enable the firm to identify threats to independence during the period of the engagement and during the period covered by the subject matter.
 - communicate circumstances and relationships that may create a threat to independence so that the firm can evaluate whether such a threat is at an acceptable level and, if it is not, address the threat by eliminating it or reducing it to an acceptable level.
 - promptly communicate any breaches of the relevant ethical requirements, including those related to independence.

A41. The engagement partner may take into account the information, communication, and resources described in paragraph A39 when determining whether the engagement partner may depend on the firm's policies or procedures in complying with relevant ethical requirements.

A42. Open and robust communication between the members of the engagement team about relevant ethical requirements may also assist in

- drawing the attention of engagement team members to relevant ethical requirements that may be of particular significance to the audit engagement, and
- keeping the engagement partner informed about matters relevant to the engagement team's understanding and fulfillment of relevant ethical requirements and the firm's related policies or procedures.

Identifying and Evaluating Threats to Compliance With Relevant Ethical Requirements (Ref: par. 17-18)

A43. In accordance with SQMS No. 1, the firm's responses to address the quality risks in relation to relevant ethical requirements, including those related to independence for engagement team members, include policies or procedures for identifying, evaluating, and addressing threats to compliance with the relevant ethical requirements.

A44. Relevant ethical requirements may contain provisions regarding the identification and evaluation of threats and how they are to be dealt with. For example, the “General Requirements for Performing Nonattest Services” interpretation (ET sec. 1.295.040) of the “Independence Rule” in the AICPA code provides guidance regarding safeguards for reducing threats to independence to an acceptable level when performing nonattest services for an attest client.

Breaches of Relevant Ethical Requirements (Ref: par. 19)

A45. In accordance with SQMS No. 1, the firm is required to establish policies or procedures for identifying, communicating, evaluating, and reporting ~~of~~ any breaches of relevant ethical requirements and appropriately responding to the causes and consequences of the breaches in a timely manner.

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Taking Appropriate Action (Ref: par. 20)

A46. Examples of appropriate actions may include the following:

- Following the firm’s policies or procedures regarding breaches of relevant ethical requirements, including communicating to or consulting with the appropriate individuals so that appropriate action can be taken, including as applicable, disciplinary action.
- Communicating with those charged with governance.
- Communicating with regulatory authorities or professional bodies. In some circumstances, communication with regulatory authorities may be required by law or regulation.
- Seeking legal advice.
- Withdrawing from the audit engagement, when withdrawal is possible under applicable law or regulation.

Prior to Dating the Auditor’s Report (Ref: par. 21)

A47. AU-C section 700, *Forming an Opinion and Reporting on Financial Statements*, requires that the auditor’s report include a statement that the auditor is independent of the entity in accordance with the relevant ethical requirements relating to the audit and that the auditor has fulfilled the auditor’s other ethical responsibilities in accordance with these requirements.²⁸ Performing the procedures required by paragraphs 16–21 of this ~~proposed~~ SAS provides the basis for these statements in the auditor’s report.

Considerations Specific to Governmental Audit Organizations

A48. Law or regulation may provide safeguards for the independence of governmental audit organizations and the auditors they employ. However, in the absence of law or regulation, governmental audit organizations may establish supplemental safeguards to assist the auditor or audit organization in maintaining independence. Additionally, when law or regulation does not permit withdrawal from the engagement, the auditor may disclose in the auditor’s report the circumstances affecting the auditor’s independence.

Acceptance and Continuance of Client Relationships and Audit Engagements (Ref: par. 22–24)

A49. ~~Proposed SQMS A Firm’s System of Quality Management~~ SQMS No. 1 requires the firm to establish quality objectives that address the acceptance and continuance of client relationships and specific engagements.

²⁸ Paragraph .28c of AU-C section 700.

A50. Information such as the following may assist the engagement partner in determining whether the conclusions reached regarding the acceptance and continuance of client relationships and audit engagements are appropriate:

- The integrity and ethical values of the principal owners, key management, and those charged with governance of the entity
- Whether sufficient and appropriate resources are available to perform the engagement
- Whether management and those charged with governance have acknowledged their responsibilities in relation to the engagement
- Whether the engagement team has the competence and capabilities, including sufficient time, to perform the engagement
- Whether significant matters that have arisen during the current or previous engagement have implications for continuing the engagement

A51. Under ~~proposed SQMS A Firm's System of Quality Management~~ **SQMS No. 1**, for acceptance and continuance decisions, the firm is required to make judgments about the firm's ability to perform the engagement in accordance with professional standards and applicable legal and regulatory requirements. The engagement partner may use the information considered by the firm in this regard in determining whether the conclusions reached regarding the acceptance and continuance of client relationships and audit engagements are appropriate. If the engagement partner has concerns regarding the appropriateness of the conclusions reached, the engagement partner may discuss the basis for those conclusions with those involved in the acceptance and continuance process.

A52. If the engagement partner is directly involved throughout the firm's acceptance and continuance process, the engagement partner will be aware of the information obtained or used by the firm in reaching the related conclusions. Such direct involvement may also provide a basis for the engagement partner's determination that the firm's policies or procedures have been followed and that the conclusions reached are appropriate.

A53. Information obtained during the acceptance and continuance process may assist the engagement partner in complying with the requirements of this ~~proposed~~ SAS and making informed decisions about appropriate courses of action. Such information may include the following:

- Information about the size, complexity, and nature of the entity, including whether it is a group audit, the industry in which it operates, and the applicable financial reporting framework
- The entity's timetable for reporting, such as at interim and final stages
- In relation to group audits, the nature of the control relationships between the parent and its components
- Whether there have been changes in the entity or in the industry in which the entity operates since the previous audit engagement that may affect the nature of resources required, as well as the manner in which the work of the engagement team will be directed, supervised, and reviewed

A54. Information obtained during acceptance and continuance may also be relevant in complying with the requirements of other AU-C sections, as well as this ~~proposed~~ SAS, for example, with respect to the following:

- Establishing an understanding of the terms of the audit engagement, as required by AU-C section 210, *Terms of Engagement*²⁹
- Identifying and assessing risks of material misstatement, whether due to error or fraud, in accordance with AU-C section 315 and AU-C section 240, *Consideration of Fraud in a Financial Statement Audit*
- Understanding the group, its components, and their environments, in the case of an audit of group financial statements in accordance with AU-C section 600, and directing, supervising, and reviewing the work of component auditors
- Determining whether, and how, to involve an auditor's specialist in accordance with AU-C section 620
- The entity's governance structure in accordance with AU-C section 260, *The Auditor's Communication With Those Charged With Governance*, and AU-C section 265, *Communicating Internal Control Related Matters Identified in an Audit*

A55. Law, regulation, or relevant ethical requirements may require the successor auditor to request, prior to accepting the audit engagement, the predecessor auditor to provide known information regarding any facts or circumstances that, in the predecessor auditor's judgment, the successor auditor needs to be aware of before deciding whether to accept the engagement. In some circumstances, the predecessor auditor may be required, on request by the proposed successor auditor, to provide information regarding identified or suspected noncompliance with laws and regulations to the proposed successor auditor.

A56. In circumstances **whenin which** the firm is obligated by law or regulation to accept or continue an audit engagement, the engagement partner may take into account information obtained by the firm about the nature and circumstances of the engagement.

A57. In deciding on the necessary action, the engagement partner and the firm may conclude that it is appropriate to continue with the audit engagement and, if so, determine what additional steps are necessary at the engagement level (for example, the assignment of more staff or staff with specific expertise). If the engagement partner has further concerns or is not satisfied that the matter has been appropriately resolved, the firm's policies or procedures for resolving differences of opinion may be applicable.

Considerations Specific to Governmental Audit Organizations (Ref: par. 22–24)

A58. When the auditor is a government audit organization, the auditor may be appointed in accordance with law or regulation, and the auditor may not need to establish all policies or procedures regarding the acceptance and continuance of audit engagements. Nevertheless, the requirements and considerations for the acceptance and continuance of client relationships and engagements as set out in paragraphs 22–24 and A48–A56 may be valuable to such auditors in performing risk assessments and in carrying out reporting responsibilities.

Engagement Resources (Ref: par. 25–28)

A59. Under **proposed SQMS A Firm's System of Quality Management SQMS No. 1**, the resources assigned or made available by the firm to support the performance of audit engagements include

- human resources,
- technological resources, and
- intellectual resources.

²⁹ Paragraph .09 of AU-C section 210, *Terms of Engagement*.

A60. Resources for an audit engagement are primarily assigned or made available by the firm, although there may be circumstances when in which the engagement team directly obtains resources for the audit engagement. For example, this may be the case when a component auditor is required by statute, regulation, or for another reason to express an audit opinion on the financial statements of a component, and the component auditor is also appointed by component management to perform audit procedures on behalf of the group engagement team.³⁰ In such circumstances, the firm's policies or procedures may require the engagement partner to take different actions, such as requesting information from the component auditor, to determine whether sufficient and appropriate resources are assigned or made available.

A61. A relevant consideration for the engagement partner, in complying with the requirements in paragraphs 25 and 26, may be whether the resources assigned or made available to the engagement team enable fulfillment of relevant ethical requirements, including ethical principles such as professional competence and due care.

Human Resources

A62. Human resources include members of the engagement team (see also paragraphs A5 and A15–A21) and, when applicable, an auditor's external specialist and individuals from within the entity's internal audit function who provide direct assistance on the audit.

Technological Resources

A63. The use of technological resources on the audit engagement may assist the auditor in obtaining sufficient appropriate audit evidence. Technological resources may include tools that allow the auditor to more effectively and efficiently manage the audit. Technological tools may also allow the auditor to evaluate large amounts of data more easily to, for example, provide deeper insights, identify unusual trends, or more effectively challenge management's assertions, which enhances the ability of the auditor to exercise professional skepticism. Technological tools may also be used to conduct meetings and provide communication tools to the engagement team. Inappropriate use of technological resources may, however, increase the risk of overreliance on the information produced for decision-making purposes or may create threats to complying with relevant ethical requirements, for example, requirements related to confidentiality.

A64. The firm's policies or procedures may include required considerations or responsibilities for the engagement team when using firm-approved technological tools to perform audit procedures and may require, depending on the tool used, the involvement of individuals with specialized skills or expertise in evaluating or analyzing the output.

A65. When the engagement partner requires individuals from another firm to use specific automated tools and techniques when performing audit procedures, communications with those individuals may indicate that the use of such automated tools and techniques needs to comply with the engagement team's instructions.

A66. The firm's policies or procedures may specifically prohibit the use of certain IT applications or features of IT applications (for example, software that has not yet been specifically approved for use by the firm). Alternatively, the firm's policies or procedures may require the engagement team to take certain actions before using an IT application that is not firm -approved to determine it is appropriate for use, for example, by requiring

- the engagement team to have appropriate competence and capabilities to use the technological resource.
- testing of the operation and security of the IT application.
- specific documentation to be included in the audit file.

³⁰ See paragraph .03 of AU-C section 600, *Special Considerations — Audits of Group Financial Statements (Including the Work of Component Auditors)*.

A67. The engagement partner may exercise professional judgment in considering whether the use of an IT application on the audit engagement is appropriate in the context of the engagement, and if so, how the IT application is to be used. Factors that may be considered in determining whether a particular IT application that has not been specifically approved for use by the firm is appropriate for use in the audit engagement include whether

- use and security of the IT application ~~complies~~comply with the firm's policies or procedures.
- the IT application operates as intended.
- personnel have the competence and capabilities required to use the IT application.

Intellectual Resources

A68. Intellectual resources include, for example, audit methodologies, implementation tools, auditing guides, model programs, templates, checklists, or forms.

A69. The use of intellectual resources on the audit engagement may facilitate the consistent application and understanding of professional standards, law and regulation, and related firm policies or procedures. For this purpose, the engagement team may be required, in accordance with the firm's policies or procedures, to use the firm's audit methodology and specific tools and guidance. The engagement team may also consider whether the use of other intellectual resources is appropriate and relevant based on the nature and circumstances of the engagement, for example, an industry-specific methodology or related guides and performance aids.

Sufficient and Appropriate Resources to Perform the Engagement (Ref: par. 25)

A70. In determining whether sufficient and appropriate resources to perform the engagement have been assigned or made available to the engagement team, ordinarily, the engagement partner may depend on the firm's related policies or procedures (including resources) as described in paragraph A6. For example, based on information communicated by the firm, the engagement partner may be able to depend on the firm's technological development, implementation, and maintenance programs when using firm-approved technology to perform audit procedures.

~~A70~~**A71.** The engagement partner may find it necessary to seek input from others with responsibilities for direction, supervision, and review to make the determinations required by paragraphs 25–27 of this ~~proposed~~SAS.

Competence and Capabilities of the Engagement Team (Ref: par. 26)

~~A71~~**A72.** When determining that the engagement team has the appropriate competence and capabilities, the engagement partner may take into consideration such matters as the team's

- understanding of, and practical experience with, audit engagements of a similar nature and complexity through appropriate training and participation.
- understanding of professional standards and applicable legal and regulatory requirements.
- expertise in specialized areas of accounting or auditing.
- expertise in IT used by the entity or automated tools or techniques that are to be used by the engagement team in planning and performing the audit engagement.
- knowledge of relevant industries in which the entity being audited operates.
- ability to exercise professional skepticism and professional judgment.
- understanding of the firm's policies or procedures.

A72A73. Internal auditors and an auditor's external specialist are not members of the engagement team. AU-C section 610³¹ and AU-C section 620³² include requirements and guidance relating to the assessment of the competence and capabilities of internal auditors and an auditor's external specialist, respectively.

Project Management

A73A74. In situations in which there are many engagement team members, for example, in an audit of a larger or more complex entity, the engagement partner may involve an individual who has specialized skills or knowledge in project management, supported by appropriate technological and intellectual resources of the firm. Conversely, in an audit of a less complex entity with few engagement team members, project management may be achieved by a member of the engagement team through less formal means.

A74A75. Project management techniques and tools may support the engagement team in managing the quality of the audit engagement by, for example,

- increasing the engagement team's ability to exercise professional skepticism through alleviating budget or time constraints that may otherwise impede the exercise of professional skepticism;
- facilitating timely performance of audit work to effectively manage time constraints at the end of the audit process when more difficult or contentious matters may arise;
- monitoring the progress of the audit against the audit plan,³³ including the achievement of key milestones, which may assist the engagement team in being proactive in identifying the need for making timely adjustments to the audit plan and the assigned resources;
- facilitating communication among members of the engagement team, for example, coordinating arrangements with component auditors and auditor's experts.

Insufficient or Inappropriate Resources (Ref: par. 27)

A75. ~~Proposed SQMS A Firm's System of Quality Management~~**A76. SQMS No. 1** addresses the firm's commitment to quality through its culture that exists throughout the firm, which recognizes and reinforces the firm's role in serving the public interest by consistently performing quality engagements, and the importance of quality in the firm's strategic decisions and actions, including the firm's financial and operational priorities. ~~Proposed SQMS A Firm's System of Quality Management~~**SQMS No. 1** also addresses the firm's responsibilities for planning for resource needs and obtaining, allocating, or assigning resources in a manner that is consistent with the firm's commitment to quality. However, in certain circumstances, the firm's financial and operational priorities may place constraints on the resources assigned or made available to the engagement team. In such circumstances, these constraints do not override the engagement partner's responsibility for achieving quality at the engagement level, including for determining that the resources assigned or made available by the firm are sufficient and appropriate to perform the audit engagement.

A76A77. In an audit of group financial statements, when there are insufficient or inappropriate resources in relation to work being performed at a component by a component auditor, the engagement partner may discuss the matter with the component auditor, management, or the firm to make sufficient and appropriate resources available.

A77A78. The engagement partner's determination of whether additional engagement level resources are required is a matter of professional judgment and is influenced by the requirements of this ~~proposed~~SAS and the nature and circumstances of the audit engagement. As described in paragraph A11,

³¹ Paragraph .13 of AU-C section 610.

³² Paragraph .09 of AU-C section 620.

³³ See paragraph .09 of AU-C section 300.

in certain circumstances, the engagement partner may determine that the firm's responses to quality risks are ineffective in the context of the specific engagement, including that certain resources assigned or made available to the engagement team are insufficient. In those circumstances, the engagement partner is required to take appropriate action, including communicating such information to the appropriate individuals in accordance with paragraph 27 and paragraph 39c. For example, if an audit software program provided by the firm has not incorporated new or revised audit procedures regarding recently issued industry regulation, timely communication of such information to the firm enables the firm to take steps to update and reissue the software promptly or to provide an alternative resource that enables the engagement team to comply with the new regulation in the performance of the audit engagement.

A78A79. If the resources assigned or made available are insufficient or inappropriate in the circumstances of the engagement and additional or alternative resources have not been made available, appropriate actions may include the following:

- Changing the planned approach to the nature, timing, and extent of direction, supervision, and review (see also paragraph A94)
- Discussing an extension to reporting deadlines with management or those charged with governance, when an extension is possible under applicable law or regulation
- Following the firm's policies or procedures for resolving differences of opinion if the engagement partner does not obtain the necessary resources for the audit engagement
- Following the firm's policies or procedures for withdrawing from the audit engagement, when withdrawal is possible under applicable law or regulation

Considerations Specific to Audits of Governmental Entities (Ref: par. 25–28)

A79A80. For audits of governmental entities, competence may include skills that are necessary to comply with applicable law or regulation, such as knowledge of *Government Auditing Standards* and an understanding of the applicable reporting requirements, including reporting to the legislature or other governing body or reporting in the public interest. The scope of a governmental audit may include, for example, additional requirements with respect to detecting misstatements that result from violations of provisions of contracts or grant agreements that could have a direct and material effect ~~on~~ the determination of financial statement amounts or the need to examine and report on internal control over financial reporting or compliance.

Engagement Performance

Scalability (Ref: par. 29)

A80A81. When an audit is not carried out entirely by the engagement partner, or in an audit of an entity whose nature and circumstances are more complex, it may be necessary for the engagement partner to assign direction, supervision, and review to other members of the engagement team. However, as part of the engagement partner's overall responsibility for managing and achieving quality on the audit engagement and to be sufficiently and appropriately involved, the engagement partner is required to determine that the nature, timing, and extent of direction, supervision, and review is undertaken in accordance with paragraph 30. In such circumstances, personnel or members of the engagement team, including component auditors, may provide information to the engagement partner to enable the engagement partner to make the determination required by paragraph 30.

Direction, Supervision, and Review (Ref: par. 30)

A81A82. Under ~~proposed~~-SQMS ~~A Firm's System of Quality Management~~~~No. 1~~, the firm is required to establish a quality objective that addresses the nature, timing, and extent of the direction and supervision of engagement teams and review of their work. ~~Proposed~~-SQMS ~~A Firm's System of Quality Management~~~~No. 1~~ also requires that such direction, supervision, and review ~~is~~~~be~~ planned and performed on the basis that the work performed by less experienced members of the engagement team ~~is~~~~be~~ directed, supervised, and reviewed by more experienced engagement team members.

A82A83. Direction and supervision of the engagement team and the review of the work of the engagement team are firm-level responses that are implemented at the engagement level, of which the nature, timing, and extent may be further tailored by the engagement partner in managing the quality of the audit engagement. Accordingly, the approach to direction, supervision, and review will vary from one engagement to the next, taking into account the nature and circumstances of the engagement. The approach will generally include a combination of addressing the firm's policies or procedures and engagement-specific responses.

A83A84. The approach to the direction and supervision of the members of the engagement team and the review of their work provides support for the engagement partner in fulfilling the requirements of this ~~proposed~~ SAS and in concluding that the engagement partner has been sufficiently and appropriately involved throughout the audit engagement in accordance with paragraph 40.

A84A85. Ongoing discussion and communication among members of the engagement team allows less experienced engagement team members to raise questions with more experienced engagement team members (including the engagement partner) in a timely manner and enables effective direction, supervision, and review in accordance with paragraph 30.

Direction

A85A86. Direction of the engagement team may involve informing the members of the engagement team of their responsibilities, such as the following:

- Contributing to the management and achievement of quality at the engagement level through their personal conduct, communication, and actions
- Maintaining a questioning mind and being aware of unconscious or conscious auditor biases in maintaining professional skepticism when gathering and evaluating audit evidence (see paragraph A35)
- Fulfilling relevant ethical requirements
- The responsibilities of respective partners when more than one partner is involved in the conduct of an audit engagement
- The responsibilities of respective engagement team members to perform audit procedures and of more experienced engagement team members to direct, supervise, and review the work of less experienced engagement team members
- Understanding the objectives of the work to be performed and the detailed instructions regarding the nature, timing, and extent of planned audit procedures as set forth in the overall audit strategy and audit plan
- Addressing threats to the achievement of quality, and the engagement team's expected response, for example, the threat that budget constraints or resource constraints result in the engagement team members inappropriately modifying planned audit procedures or failing to perform planned audit procedures

Supervision

A86A87. Supervision may include matters such as the following:

- Tracking the progress of the audit engagement, which includes monitoring
 - the progress against the audit plan;²
 - whether the objective of work performed has been achieved;² and

- the ongoing adequacy of assigned resources
- Taking appropriate action to address issues arising during the engagement, including, for example, reassigning planned audit procedures to more experienced engagement team members when issues are more complex than initially anticipated
- Identifying matters for consultation or consideration by more experienced engagement team members during the audit engagement
- Providing coaching and on-the-job training to help engagement team members develop skills or competencies
- Creating an environment where engagement team members raise concerns without fear of reprisals

Review

A87. Review of the engagement team's work provides support for the conclusion that the requirements of this ~~proposed~~ SAS have been addressed.

A88A89. Review of the engagement team's work consists of consideration of whether, for example,

- the work has been performed in accordance with the firm's policies or procedures, professional standards, and applicable legal and regulatory requirements;
- significant matters have been raised for further consideration;
- appropriate consultations have taken place, and the resulting conclusions have been documented and implemented;
- there is a need to revise the nature, timing, and extent of work performed;
- the work performed supports the conclusions reached and is appropriately documented;
- the evidence obtained is sufficient and appropriate to provide a basis for the auditor's opinion; and
- the objectives of the audit procedures have been achieved.

A89A90. The firm's policies or procedures may contain specific requirements regarding

- the nature, timing, and extent of review of audit documentation;
- different types of review that may be appropriate in different situations (for example, review of each individual working paper or selected working papers); and
- which members of the engagement team are required to perform the different types of review.

The Engagement Partner's Review (Ref: par. 30–34)

A90A91. As required by AU-C section 300, the engagement partner reviews the overall audit strategy and audit plan.³⁴ As required by AU-C section 230, the engagement partner documents the date and extent of the review.³⁵

³⁴ Paragraph .11 of AU-C section 300, as amended by this SAS.

³⁵ Paragraph .09c of AU-C section 230.

A91A92. Timely review of documentation by the engagement partner at appropriate stages throughout the audit engagement enables significant matters to be resolved to the engagement partner's satisfaction on or before the date of the auditor's report. The engagement partner need not review all audit documentation. The engagement partner exercises professional judgment in determining the extent of documentation to be reviewed, for example, when determining the nature and extent of the review of component auditor documentation in a group audit.

A92A93. The engagement partner exercises professional judgment in identifying the areas of significant judgment made by the engagement team. The firm's policies or procedures may specify certain matters that are commonly expected to be significant judgments. Significant judgments in relation to the audit engagement may include matters related to the overall audit strategy and audit plan for undertaking the engagement, the execution of the engagement, and the overall conclusions reached by the engagement team. Examples follow:

- Matters related to planning the engagement, such as matters related to determining materiality
 - The composition of the engagement team, including
 - personnel using expertise in a specialized area of accounting or auditing
 - the use of personnel from service delivery centers
 - The decision to involve an auditor's specialist, including the decision to involve an external specialist
- The engagement team's consideration of information obtained in the acceptance and continuance process and proposed responses to that information
- The engagement team's risk assessment process, including situations in which consideration of inherent risk factors and the assessment of inherent risk requires significant judgment by the engagement team
- The engagement team's consideration of related party relationships and transactions and disclosures
- Results of the procedures performed by the engagement team on significant areas of the engagement, for example, conclusions concerning certain accounting estimates, accounting policies, or going concern considerations
- The engagement team's evaluation of the work performed by specialists and conclusions drawn therefrom
- In group audit situations:
 - the proposed overall group audit strategy and group audit plan;
 - decisions about the involvement of component auditors, including how to direct and supervise them and review their work, including, for example, when there are areas of higher assessed risk of material misstatement of the financial information of a component; and
 - the evaluation of work performed by component auditors and the conclusions drawn therefrom
- How matters affecting the overall audit strategy and audit plan have been addressed

- The significance and disposition of corrected and uncorrected misstatements identified during the engagement
- The proposed audit opinion and matters to be communicated in the auditor's report, for example, key audit matters, or a "Material Uncertainty Related to Going Concern" paragraph-

A93A94. The engagement partner exercises professional judgment in determining other matters to review, for example, based on

- the nature and circumstances of the audit engagement.
- which engagement team member performed the work.
- matters relating to recent inspection findings.
- the requirements of the firm's policies or procedures.

Nature, Timing, and Extent

A94A95. The nature, timing, and extent of the direction, supervision, and review are required to be planned and performed in accordance with the firm's policies or procedures, as well as professional standards and applicable legal and regulatory requirements. For example, the firm's policies or procedures may include the following:

- Work planned to be performed at an interim date is to be directed, supervised, and reviewed at the same time as the performance of the procedures, rather than at the end of the period, so that any necessary corrective action can be taken in a timely manner.
- Certain matters are to be reviewed by the engagement partner, and the firm may specify the circumstances or engagements in which such matters are expected to be reviewed.

Scalability

A95A96. The following are examples of factors that may influence the firm's approach to direction, supervision, and review:

- The engagement team member's previous experience with the entity and the area to be audited. For example, if the work related to the entity's information system is being performed by the same engagement team member who performed the work in the prior period and there are no significant changes to the information system, the extent and frequency of the direction and supervision of the engagement team member may be less, and the review of the related working papers may be less detailed.
- The complexity of the audit engagement. For example, if significant events have occurred that make the audit engagement more complex, the extent and frequency of the direction and supervision of the engagement team member may be greater, and the review of the related working papers may be more detailed.
- The assessed risks of material misstatement. For example, a higher assessed risk of material misstatement may require a corresponding increase in the extent and frequency of the direction and supervision of engagement team members and a more detailed review of their work.

- The competence and capabilities of the individual engagement team members performing the audit work. For example, less experienced engagement team members may require more detailed instructions and more frequent, or in-person, interactions as the work is performed.
- The manner in which the reviews of the work performed are expected to take place. For example, in some circumstances, remote reviews may not be effective in providing the necessary direction and may need to be supplemented by in-person interactions.
- The structure of the engagement team and the location of engagement team members. For example, direction and supervision of individuals located at service delivery centers and the review of their work may
 - be more formalized and structured than when members of the engagement team are all situated in the same location; or
 - use IT to facilitate the communication between the members of the engagement team.

A96A97. Identification of changes in the engagement circumstances may warrant reevaluation of the planned approach to the nature, timing, or extent of direction, supervision, or review. For example, if the assessed risk of material misstatement at the financial statement level increases because of a complex transaction, the engagement partner may need to change the planned level of review of the work related to the transaction.

A97A98. In accordance with paragraph 30b, the engagement partner is required to determine that the approach to direction, supervision, and review is responsive to the nature and circumstances of the audit engagement. For example, if a more experienced engagement team member becomes unavailable to participate in the supervision and review of the engagement team, the engagement partner may need to increase the extent of supervision and review of the less experienced engagement team members.

Review of Communications to Management, Those Charged With Governance, or Regulatory Authorities (Ref: par. 34)

A98A99. The engagement partner uses professional judgment in determining which written communications to review, taking into account the nature and circumstances of the audit engagement. For example, it may not be necessary for the engagement partner to review communications between the engagement team and management in the ordinary course of the audit.

Consultation (Ref: par. 35)

A99. ~~Proposed SQMS A Firm's System of Quality Management~~ **A100. SQMS No. 1** requires the firm to establish a quality objective that addresses consultation on difficult or contentious matters and how the conclusions agreed are implemented. Consultation may be appropriate or required, for example, for

- issues that are complex or unfamiliar (for example, issues related to an accounting estimate with a high degree of estimation uncertainty),
- significant risks,
- significant transactions that are outside the normal course of business for the entity or that otherwise appear to be unusual,
- limitations imposed by management, and
- noncompliance with laws or regulations.

A100A101. Effective consultation on significant technical, ethical, and other matters within the firm or, where applicable, outside the firm, may be achieved when those consulted

- are given all the relevant facts that will enable them to provide informed advice and
- have appropriate knowledge, seniority, and experience.

A104A102. It may be appropriate for the engagement team, in the context of the firm's policies or procedures, to consult outside the firm, for example, in areas where the firm lacks appropriate internal resources. The engagement team may take advantage of advisory services provided by firms, professional and regulatory bodies, or commercial organizations that provide relevant quality control services.

A102A103. The need for consultation outside the engagement team on a difficult or contentious matter may be an indicator that the matter is a key audit matter.³⁶

Engagement Quality Review (Ref: par. 36)

~~A103. Proposed SQMS A Firm's System of Quality Management~~**A104. SQMS No. 1** contains requirements that the firm establish policies or procedures addressing engagement quality reviews in accordance with ~~proposed SQMS No. 2, Engagement Quality Reviews~~³⁷ and requiring an engagement quality review for certain types of engagements.³⁸ ~~Proposed SQMS Engagement Quality Reviews~~**SQMS No. 2** deals with the appointment and eligibility of the engagement quality reviewer and the engagement quality reviewer's responsibilities relating to performing and documenting an engagement quality review.

Completion of the Engagement Quality Review Before Dating of the Auditor's Report (Ref: par. 36d)

A104A105. AU-C section 700 requires the auditor's report to be dated no earlier than the date on which the auditor has obtained sufficient appropriate audit evidence on which to base the auditor's opinion on the financial statements.³⁹ If applicable to the audit engagement, ~~proposed SQMS Engagement Quality Reviews~~**No. 2** and this ~~proposed~~ SAS require that the engagement partner be precluded from releasing the engagement report until notification has been received from the engagement quality reviewer that the engagement quality review is complete. For example, if the engagement quality reviewer has communicated to the engagement partner concerns about the significant judgments made by the engagement team or that the conclusions reached thereon were not appropriate, then the engagement quality review is not complete.⁴⁰

A105A106. An engagement quality review that is conducted in a timely manner at appropriate stages during the audit engagement may assist the engagement team in promptly resolving matters raised to the engagement quality reviewer's satisfaction on or before the date of the auditor's report.

A106A107. Frequent communications between the engagement team and the engagement quality reviewer throughout the audit engagement may assist in facilitating an effective and timely engagement quality review. In addition to discussing significant matters with the engagement quality reviewer, the engagement partner may assign responsibility for coordinating requests from the engagement quality reviewer to another member of the engagement team.

Differences of Opinion (Ref: par. 37–38)

~~A107. Proposed SQMS A Firm's System of Quality Management~~**A108. SQMS No. 1** requires the firm to establish a quality objective that addresses differences of opinion that arise within the engagement team or between the engagement team and the engagement quality reviewer or individuals performing activities within the firm's system of quality management. ~~Proposed SQMS A Firm's System of Quality Management~~**No. 1** also requires that differences of opinion ~~are~~**be** brought to the attention of the firm and

³⁶ Paragraphs .09 and .A13b of AU-C section 701.

³⁷ SQMS No. 2, *Engagement Quality Reviews*.

³⁸ Paragraph 35f of SQMS No. 1.

³⁹ Paragraph .43 of AU-C section 700.

⁴⁰ Paragraph 21b of SQMS No. 2.

resolved. For example, a component auditor may be instructed to communicate differences of opinion to the group engagement team.

A408A109. In some circumstances, the engagement partner may not be satisfied with the resolution of the difference of opinion. In such circumstances, appropriate actions for the engagement partner may include, for example,

- seeking legal advice or
- withdrawing from the audit engagement, when withdrawal is possible under applicable law or regulation.

Monitoring and Remediation (Ref: par. 39)

A409. ~~Proposed A110.~~ SQMS *A Firm's System of Quality Management* ~~No. 1~~ sets out requirements for the firm's monitoring and remediation process. ~~Proposed SQMS A Firm's System of Quality Management~~ ~~SQMS No. 1~~ requires the firm to communicate to engagement teams information about the firm's monitoring and remediation process to enable them to take prompt and appropriate action in accordance with their responsibilities. Further, information provided by members of the engagement team may be used by the firm in the firm's monitoring and remediation process, and exercising professional judgment and maintaining professional skepticism while conducting the audit may assist the members of the engagement team in remaining alert for information that may be relevant to that process.

A440A111. Information provided by the firm may be relevant to the audit engagement when, for example, it relates to findings on another engagement performed by the engagement partner or other members of the engagement team, findings from the local firm office, or inspection results of previous audits of the entity.

A444A112. In considering information communicated by the firm through its monitoring and remediation process and how it may affect the audit engagement, the engagement partner may consider the remedial actions designed and implemented by the firm to address deficiencies and, to the extent relevant to the nature and circumstances of the engagement, communicate accordingly to the engagement team. The engagement partner may also determine whether additional remedial actions are needed at the engagement level. For example, the engagement partner may determine that

- an auditor's specialist is needed, or
- the nature, timing, and extent of direction, supervision, and review ~~needs~~need to be enhanced in an area of the audit where deficiencies have been identified.

If an identified deficiency does not affect the quality of the audit (for example, if it relates to a technological resource that the engagement team did not use), then no further action may be needed.

A442A113. A deficiency in the firm's system of quality management does not necessarily indicate that an audit engagement was not performed in accordance with professional standards and applicable legal and regulatory requirements or that the auditor's report was not appropriate in the circumstances.

Taking Overall Responsibility for Managing and Achieving Quality (Ref: par. 40)

A413. ~~Proposed SQMS A Firm's System of Quality Management~~ **A114.** SQMS No. 1 requires the firm to establish a quality objective addressing the engagement team's understanding and fulfillment of their responsibilities in connection with the engagement. ~~Proposed SQMS A Firm's System of Quality~~

~~Management~~~~SQMS No. 1~~ further requires that the quality objective include the overall responsibility of engagement partners for managing and achieving quality on the engagement and being sufficiently and appropriately involved throughout the engagement.

~~A114~~~~A115~~. Relevant considerations in addressing paragraph 40 include determining how the engagement partner has complied with the requirements of this ~~proposed~~ SAS, given the nature and circumstances of the audit engagement and how the audit documentation evidences the engagement partner's involvement throughout the audit engagement, as described in paragraph A118.

~~A115~~~~A116~~. Indicators that the engagement partner may not have been sufficiently and appropriately involved include, for example, the following:

- Lack of timely review by the engagement partner of the audit engagement planning, including reviewing the assessment of risks of material misstatement and the design of ~~these~~ responses to those risks ~~towardstoward~~ the end of the audit
- Evidence that assignees were not provided necessary instructions and relevant information, such as not being adequately informed about the nature of their responsibilities and authority, the scope of the work being assigned, and the objectives thereof
- A lack of evidence of the engagement partner's direction and supervision of the other members of the engagement team and the review of their work

~~A116~~~~A117~~. If the engagement partner's involvement does not provide the basis for determining that the significant judgments made and the conclusions reached are appropriate, the engagement partner will not be able to reach the determination required by paragraph 40. In addition to ~~applying-taking into account~~ firm policies or procedures that may set forth the required actions to be taken in such circumstances, appropriate actions that the engagement partner may take, include, for example,

- updating and changing the audit plan,
- reevaluating the planned approach to the nature and extent of review and modifying the planned approach to increase the involvement of the engagement partner, or
- consulting with personnel assigned operational responsibility for the relevant aspect of the firm's system of quality management.

Documentation (Ref: par. 41)

~~A117~~~~A118~~. In accordance with AU-C section 230,⁴¹ audit documentation provides evidence that the audit complies with GAAS. However, it is neither necessary nor practicable for the auditor to document every matter considered, or professional judgment made, in an audit. Further, it is unnecessary for the auditor to document separately (~~such as in a checklist, for example~~) compliance with matters for which compliance is demonstrated by documents included within the audit file.

~~A118~~~~A119~~. Documentation of the performance of the requirements of this ~~proposed~~ SAS, including evidencing the involvement of the engagement partner and the engagement partner's determination in accordance with paragraph 40, may be accomplished in different ways depending on the nature and circumstances of the audit engagement. Examples follow:

- Direction of the engagement team can be documented through sign-offs of the audit plan and project management activities.

Commented [AG31]: Change directed by ASB at January meeting, to revert to original wording

⁴¹ Paragraph .A9 of AU-C section 230.

- Minutes from formal meetings of the engagement team may provide evidence of the clarity, consistency, and effectiveness of the engagement partner's communications and other actions regarding culture and expected behaviors that demonstrate the firm's commitment to quality.
- Agendas from discussions between the engagement partner and other members of the engagement team and, when applicable, the engagement quality reviewer, and related sign-offs and records of the time the engagement partner spent on the engagement, may provide evidence of the engagement partner's involvement throughout the audit engagement and supervision of other members of the engagement team.
- Sign-offs by the engagement partner and other members of the engagement team provide evidence that the working papers were reviewed.

A419A120. When dealing with circumstances that may pose risks to achieving quality on the audit engagement, the exercise of professional skepticism, and the documentation of the auditor's consideration thereof, may be important. For example, if the engagement partner obtains information that may have caused the firm to decline the engagement (see paragraph 24), the documentation may include explanations of how the engagement team dealt with the circumstance.

A420A121. Documentation of consultations with other professionals that involve difficult or contentious matters that is sufficiently complete and detailed contributes to an understanding of

- the nature and scope of the issue on which consultation was sought, and
- the results of the consultation, including any decisions taken, the basis for those decisions, and how they were implemented.



Appendix – Amendments to Various Statements on Auditing Standards, as Amended, and Statement on Standards for Attestation Engagements No. 18, *Attestation Standards: Clarification and Recodification*, as Amended, section 105, *Concepts Common to All Attestation Engagements*, in *AICPA Professional Standards*

Amendment to Statement on Auditing Standards (SAS) No. 117, *Compliance Audits*, as Amended

(*Boldface italics* denotes new language. Deleted text is in ~~strikethrough~~.)

AU-C section 935, *Compliance Audits*

[No amendment to paragraphs .01–.A34.]

.A35 ~~Section 220, *Proposed Statement on Auditing Standards (SAS) No. 146, Quality Control Management for an Engagement Conducted in Accordance With Generally Accepted Auditing Standards*, requires that, on or before the date of the auditor’s report, the engagement partner **determine**, through a review of the audit documentation and discussion with the engagement team, ~~be satisfied~~ that sufficient appropriate audit evidence has been obtained to support the conclusions reached and for the auditor’s report to be issued.~~ ^{fn 20} When an engagement quality ~~control~~ review is performed, ~~section 220 *proposed Statement on Auditing Standards SAS No. 146 Quality Management for an Engagement Conducted in Accordance With Generally Accepted Auditing Standards* requires that the **engagement partner not date the** auditor’s report ~~not be~~ released ~~prior to~~ **until** the completion of the engagement quality ~~control~~ review.~~ ^{fn 21}

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^{fn 20} See paragraph ~~Paragraph 1932~~ of section 220, ~~*proposed SAS No. 146, Quality Control Management for an Engagement Conducted in Accordance With Generally Accepted Auditing Standards*~~, ~~for further discussion.~~

^{fn 21} Paragraph ~~2136d~~ of section 220 ~~*proposed SAS No. 146 Quality Control Management for an Engagement Conducted in Accordance With Generally Accepted Auditing Standards*~~.

[No further amendment to AU-C section 935.]

1. This amendment is effective for compliance audits for fiscal periods ending on or after December 15, 2025.

Amendments to Various Sections in SAS No. 122, *Statements on Auditing Standards: Clarification and Recodification*, as Amended

(***Boldface italics*** denotes new language. Deleted text is in ~~strike through~~.)

AU-C Section 200, *Overall Objectives of the Independent Auditor and the Conduct of an Audit in Accordance With Generally Accepted Auditing Standards*

[No amendment to paragraphs .01–.A19.]

.A20 QC section 10 ~~Proposed~~ ***Statement on Quality Management Standards (SQMS) No. 1, A Firm's System of Quality Control Management***, sets out the firm's responsibilities to establish and maintain its design, implement, and operate a system of quality control for audit engagements, and to establish policies and procedures designed to provide it ~~management that provides the firm~~ with reasonable assurance that the firm and its personnel ***fulfill their responsibilities in accordance with professional standards and applicable legal and regulatory requirements and conduct engagements in accordance with such standards and requirements. As part of its system of quality management, proposed SQMS No. 1 A Firm's System of Quality Management requires the firm to establish quality objectives that address the fulfillment of responsibilities in accordance*** with relevant ethical requirements, including those pertaining related to independence.^{fn 7} Section 220 ~~Proposed~~ ***Statement on Auditing Standards (SAS) No. 146, Quality Control Management for an Engagement Conducted in Accordance With Generally Accepted Auditing Standards***, addresses the engagement partner's responsibilities regarding relevant ethical requirements, ***including those related to independence. These include remaining alert for evidence of noncompliance with relevant ethical requirements by members of the engagement team, determining, in consultation with others in the firm as appropriate, the appropriate action if matters come to the engagement partner's attention, through the firm's system of quality control or otherwise, that indicate that members of the engagement team have not complied with relevant ethical requirements, and forming a conclusion on compliance with independence requirements that apply to the audit engagement.***^{fn 8} Section 220 ~~Proposed SAS No. 146 Quality Management for an Engagement Conducted in Accordance With Generally Accepted Auditing Standards~~ recognizes that ***also describes when*** the engagement team is entitled to rely on a firm's system of quality control in meeting its responsibilities with respect to quality control procedures applicable to the individual audit engagement, unless the engagement partner determines that it is inappropriate to do so based on information provided by the firm or other parties ***may depend on the firm's policies or procedures in managing and achieving quality at the engagement level.***^{fn 9}

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^{fn 7} Paragraphs 21–2530 of QC section 10 ~~proposed~~ ***Statement on Quality Management Standards (SQMS) No. 1, A Firm's System of Quality Control Management***.

^{fn 8} Paragraphs 116–1321 of section 220 ~~proposed~~ ***Statement on Auditing Standards (SAS) No. 146, Quality Control Management for an Engagement Conducted in Accordance With Generally Accepted Auditing Standards***.

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^{fn 9} Paragraph A10 of ~~proposed SAS No. 146 Quality Management for an Engagement Conducted in Accordance With Generally Accepted Auditing Standards~~.

[No amendment to paragraphs .A21–.A31. Subsequent footnotes are renumbered.]

.A32 Audit evidence is necessary to support the auditor’s opinion and report. It is cumulative in nature and is primarily obtained from audit procedures performed during the course of the audit. It may, however, also include information obtained from other sources such as previous audits (provided the auditor has determined whether changes have occurred since the previous audit that may affect its relevance to the current audit¹³) or ***through the information obtained by the firm in the acceptance or continuance of the client relationship or engagement firm’s quality control procedures for client acceptance or continuance.*** In addition to other sources inside and outside the entity, the entity’s accounting records are an important source of audit evidence. Also, information that may be used as audit evidence may have been prepared by a specialist employed or engaged by the entity. Audit evidence comprises both information that supports and corroborates management’s assertions, and any information that contradicts such assertions. In addition, in some cases, the absence of information (for example, management’s refusal to provide a requested representation) is used by the auditor, and therefore, also constitutes audit evidence. Most of the auditor’s work in forming the auditor’s opinion consists of obtaining and evaluating audit evidence.

¹³ [Footnote omitted for purposes of this exposure draft.]

[No further amendment to AU-C section 200.]

2. This amendment is effective for audits of financial statements for periods beginning on or after December 15, 2025.

AU-C Section 210, Terms of Engagement

[No amendment to paragraphs .01–.18.]

.A1 ~~Proposed Statement on Quality Management Standards No. 1, A Firm’s System of Quality Management~~, addresses the firm’s responsibilities regarding the acceptance and continuance of client relationships and specific engagements. The auditor’s responsibilities regarding relevant ethical requirements, ***including those related to independence***, in the context of the acceptance of an audit engagement, insofar as they are within the control of the auditor, are dealt with in ~~section 220~~ ***proposed Statement on Auditing Standards No. 146, Quality Management for an Engagement Conducted in Accordance With Generally Accepted Auditing Standards.*** This section addresses those matters (or preconditions) that are within the control of the entity and upon which it is necessary for the auditor and the entity’s management to agree.

[No further amendment to AU-C section 210.]

3. This amendment is effective for audits of financial statements for periods beginning on or after December 15, 2025.

AU-C Section 230, Audit Documentation

[No amendment to paragraphs .01–.02.]

.03 Audit documentation serves a number of additional purposes, including the following:

- Assisting the engagement team to plan and perform the audit
- Assisting members of the engagement team responsible for supervision to direct and supervise the audit work, and to discharge their review responsibilities in accordance with ~~section 220~~ **proposed Statement on Auditing Standards (SAS) No. 146, Quality Control Management for an Engagement Conducted in Accordance With Generally Accepted Auditing Standards**³
- Enabling the engagement team to demonstrate that it is accountable for its work by documenting the procedures performed, the audit evidence examined, and the conclusions reached
- Retaining a record of matters of continuing significance to future audits of the same entity
- Enabling the conduct of **engagement** quality ~~control~~ reviews, **other types of engagement reviews, and monitoring activities under the firm's system of quality management inspections in accordance with QC section 10, A Firm's System of Quality Control**
- Enabling the conduct of external inspections in accordance with applicable legal, regulatory, or other requirements
- Assisting an auditor who reviews a predecessor auditor's audit documentation
- Assisting auditors to understand the work performed in the prior year as an aid in planning and performing the current engagement

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³ Paragraphs ~~17–19~~ **29–33** of ~~section 220~~ **proposed Statement on Auditing Standards (SAS) No. 146, Quality Control Management for an Engagement Conducted in Accordance With Generally Accepted Auditing Standards**.

[No amendment to paragraphs .04–.A8.]

.A9 Audit documentation provides evidence that the audit complies with GAAS. However, it is neither necessary nor practicable for the auditor to document every matter considered, or professional judgment made, in an audit. Further, it is unnecessary for the auditor to document separately (as in a checklist, for example) compliance with matters for which compliance is demonstrated by documents included within the audit file. For example:

- The existence of an adequately documented audit plan demonstrates that the auditor has planned the audit.

- The existence of a signed engagement letter in the audit file demonstrates that the auditor has agreed to the terms of the audit engagement with management or, when appropriate, those charged with governance.
- An auditor’s report containing an appropriately qualified opinion on the financial statements demonstrates that the auditor has complied with the requirement to express a qualified opinion under the circumstances in accordance with GAAS.
- Regarding requirements that apply generally throughout the audit, there may be a number of ways in which compliance with them may be demonstrated within the audit file:
 - For example, there may be no single way in which the auditor’s professional skepticism is documented. But the audit documentation may nevertheless provide evidence of the auditor’s exercise of professional skepticism in accordance with GAAS. Such evidence may include specific procedures performed to corroborate management’s responses to the auditor’s inquiries.
 - Similarly, that the engagement partner has taken responsibility for the direction, ~~and supervision, and performance of the~~ **engagement team and review of their work** ^{fn 6} ~~audit in compliance with GAAS~~ may be evidenced in a number of ways within the audit documentation. This may include documentation ~~of that evidences~~ the engagement partner’s ~~timely~~ **sufficient and appropriate** involvement in ~~aspects of the audit, such as participation in the~~ **engagement team discussions**, required by section 3.15, *Understanding the Entity and Its Environment and Assessing the Risks of Material Misstatement*.^{fn 6}

^{fn 6} Paragraph 29 of ~~proposed SAS No. 146~~ **Quality Management for an Engagement Conducted in Accordance With Generally Accepted Auditing Standards**.

[No amendment to paragraphs .A10–.A14.]

~~.A15 Section 220 Proposed SAS No. 146 Quality Management for an Engagement Conducted in Accordance With Generally Accepted Auditing Standards contains requirements and guidance on the~~ ~~requires the auditor to review the audit work performed through review of the audit documentation.~~⁹ The requirement to document who reviewed the audit work performed and the extent of the review, in accordance with the firm’s policies and procedures addressing review responsibilities does not imply a need for each specific working paper to include evidence of review. The requirement, however, means documenting what audit work was reviewed, who reviewed such work, and when it was reviewed.

^{fn 9} Paragraph 0931 of section 220 ~~proposed SAS No. 146~~ **Quality Management for an Engagement Conducted in Accordance With Generally Accepted Auditing Standards**.

[No amendment to paragraphs .A16–.A22.]

Matters Arising After the Date of the Auditor’s Report (Ref: par. .14)

- .A23** Examples of rare circumstances in which the auditor performs new or additional audit procedures or draws new conclusions after the date of the auditor’s report include
- when, after the date of the auditor’s report, the auditor becomes aware of facts that existed at that date and which, if known at that date, might have caused the financial statements to be revised or the auditor to modify the opinion in the auditor’s report.^{fn 11}
 - when the auditor concludes that procedures necessary at the time of the audit, in the circumstances then existing, were omitted from the audit of the financial information.^{fn 12}

The resulting changes to the audit documentation are reviewed in accordance with the firm’s ~~quality control~~ procedures ~~as required by QC section 10~~ ***under its system of quality management.***

^{fn 11-12} [Footnotes omitted for purposes of this exposure draft.]

Assembly and Retention of the Final Audit File (Ref: par. .16–.18)

- .A24** Statutes, regulations, or the audit firm’s ~~quality control~~ policies ***or procedures under its system of quality management*** may specify a period of time shorter than 60 days following the report release date in which this assembly process is to be completed.

[No amendment to paragraphs .A25–.A26.]

- .A27** ~~Firms are required to establish policies and procedures for the retention of engagement documentation.~~^{fn 13} Statutes, regulations, or the audit firm’s ~~quality control~~ policies ***or procedures under its system of quality management*** may specify a retention period longer than five years.

^{fn 13} ~~Paragraph .50 of QC section 10.~~

- .A28** An example of a circumstance in which the auditor may find it necessary to modify existing audit documentation or add new audit documentation after file assembly has been completed is the need to clarify existing audit documentation arising from comments received during monitoring ~~inspections performed by internal~~ ***activities*** or external ~~parties~~ ***inspections.***

[No further amendment to AU-C section 230.]

4. This amendment is effective for audits of financial statements for periods beginning on or after December 15, 2025.

AU-C Section 260, *The Auditor’s Communication With Those Charged With Governance*

[No amendment to paragraphs .01–.A36.]

.A37 To the extent not already addressed by the requirements in paragraph .12*a–f* and related application material, the auditor may consider communicating about other matters discussed with, or considered by, the engagement quality control reviewer, if one has been appointed, ~~in accordance with section 220, *Quality Control for an Engagement Conducted in Accordance With Generally Accepted Auditing Standards*.~~^{in¹⁴}

^{in¹⁴} Paragraphs .21–.22 of section 220, *Quality Control for an Engagement Conducted in Accordance With Generally Accepted Auditing Standards*.

[No amendment to paragraphs .A38–.A50.]

.A51 Timely communication throughout the audit contributes to the achievement of robust two-way dialogue between those charged with governance and the auditor. However, the appropriate timing for communications will vary with the circumstances of the engagement. Considerations include the significance and nature of the matter, the importance of the matter to those charged with governance, and the action expected to be taken by those charged with governance. The following are examples of the timing of communications for certain matters:

- Communications regarding planning matters may often be made early in the audit engagement and, for an initial engagement, as part of the terms of the engagement.
- It may be appropriate to communicate significant difficulties encountered during the audit as soon as practicable if those charged with governance are able to assist the auditor in overcoming the difficulties or if the difficulties are likely to lead to a modified opinion.
- Communications regarding independence may be appropriate whenever significant judgments are made about threats to independence and related safeguards.
- When section 701 applies, the auditor may communicate preliminary views about key audit matters when discussing the planned scope and timing of the audit (see paragraph .A21); the auditor may also have more frequent communications to further discuss such matters when communicating about significant audit findings.

The following are examples of matters for which communication with those charged with governance may be important prior to issuance of the auditor’s report:

- Uncorrected misstatements accumulated by the auditor and the effect that they may have, individually or in the aggregate, on the opinion in the auditor’s report, including possible implications with respect to future financial statements

- Circumstances or relationships to which the auditor gave significant consideration relating to independence in reaching the conclusion that independence has not been impaired
- Significant findings or issues from the audit, including the auditor’s views about the qualitative aspects of the entity’s accounting practices
- An expectation by the auditor that the opinion in the auditor’s report will be modified in accordance with section 705, *Modifications to the Opinion in the Independent Auditor’s Report*¹⁶
- When section 701 applies, the matters planned to be included in the auditor’s report. ***Proposed SAS No. 146, Quality Management for an Engagement Conducted in Accordance With Generally Accepted Auditing Standards, requires the engagement partner, prior to dating the auditor’s report, to review the financial statements and the auditor’s report, including, if applicable, the description of the key audit matters and related audit documentation, to determine that the report to be issued will be appropriate in the circumstances.***

17

¹⁶ Paragraph .31 of section 705, *Modifications to the Opinion in the Independent Auditor’s Report*.

¹⁷ Paragraph 33 of ~~proposed SAS No. 146~~, *Quality Management for an Engagement Conducted in Accordance With Generally Accepted Auditing Standards*.

[Subsequent footnotes are renumbered.]

[No further amendment to AU-C section 260.]

5. This amendment is effective for audits of financial statements for periods beginning on or after December 15, 2025.

AU-C Section 300, *Planning an Audit*

Introduction

Scope of This Section

[No amendment to paragraph .01.]

~~The Role and Timing of Planning~~

.02 Planning an audit involves establishing the overall audit strategy for the engagement and developing an audit plan. Adequate ***Quality management at the engagement level in accordance with ~~proposed~~ Statement on Auditing Standards (SAS) No. 146, Quality Management for an Engagement Conducted in Accordance With Generally Accepted***

Auditing Standards, in conjunction with adequate planning in accordance with this section, benefits the audit of financial statements in several ways, including the following:

- Helping the auditor identify and devote appropriate attention to important areas of the audit
- Helping the auditor identify and resolve potential problems on a timely basis
- Helping the auditor properly organize and manage the audit engagement so that it is performed in an effective and efficient manner
- Assisting in the selection of engagement team members with appropriate levels of capabilities and competence to respond to anticipated risks and allocating team member responsibilities
- Facilitating the direction and supervision of engagement team members and the review of their work
- Assisting, when applicable, in coordination of work done by auditors of components and specialists

[No amendment to paragraphs .03–.05.]

Preliminary Engagement Activities

.06 The auditor should undertake the following activities at the beginning of the current audit engagement:

- a. Performing procedures required by ~~section 220, proposed SAS No. 146 Quality Control Management for an Engagement Conducted in Accordance With Generally Accepted Auditing Standards~~ regarding the **acceptance and continuance of the client relationship and the specific audit engagement;**
- b. Evaluating compliance with relevant ethical requirements in accordance with ~~section 220, proposed SAS No. 146 Quality Management for an Engagement Conducted in Accordance With Generally Accepted Auditing Standards~~
- c. Establishing an understanding of the terms of the engagement, as required by section 210, *Terms of Engagement*; (Ref: par. .A6–.A8)

[No amendment to paragraph .07.]

Planning Activities

.08 In establishing the overall audit strategy, the auditor should *consider the information obtained from complying with the requirements of* ~~proposed SAS No. 146 Quality Management for an Engagement Conducted in Accordance With Generally Accepted Auditing Standards~~ *and*

- a. identify the characteristics of the engagement that define its scope;

- b. ascertain the reporting objectives of the engagement to plan the timing of the audit and the nature of the communications required;
- c. consider the factors that, in the auditor’s professional judgment, are significant in directing the engagement team’s efforts;
- d. consider the results of preliminary engagement activities and, where applicable, whether knowledge gained on other engagements performed by the engagement partner for the entity is relevant; and
- e. ascertain the nature, timing, and extent of resources necessary to perform the engagement. (Ref: par. A9–A13)

.09 The auditor should develop an audit plan that includes a description of the following:

- a. ***The nature, timing, and extent of the planned direction and supervision of engagement team members and the review of their work.*** (Ref: par. ~~A18–A19~~.A14–.A15)
- b. ~~a.~~ The nature and extent of planned risk assessment procedures, as determined under section 315, *Understanding the Entity and Its Environment and Assessing the Risks of Material Misstatement*
- c. ~~b.~~ The nature, timing, and extent of planned further audit procedures at the relevant assertion level, as determined under section 330, *Performing Audit Procedures in Response to Assessed Risks and Evaluating the Audit Evidence Obtained*
- d. ~~e.~~ Other planned audit procedures that are required to be carried out so that the engagement complies with generally accepted auditing standards (Ref: par. ~~A14–A16~~.A16–.A18)

[No amendment to paragraph .10.]

.11 The auditor ***engagement partner*** should ~~plan the nature, timing, and extent of direction and supervision of engagement team members and the review of their work~~ ***review the overall audit strategy and audit plan.*** (Ref: par. ~~A18–A19~~)

[No amendment to paragraphs .12–.13.]

Documentation

.14 The auditor should include in the audit documentation the following:^{fn 3}

- a. The overall audit strategy
- b. The audit plan
- c. Any significant changes made during the audit engagement to the overall audit strategy or the audit plan, ***including any significant changes to the nature, timing, and extent of the planned direction and supervision of engagement team members***

and the review of their work,^{fn 4} and the reasons for such changes. (Ref: par. .A23–.A26)

^{fn 3} [Footnote omitted for purposes of this exposure draft.]

^{fn 4} *Paragraphs 30 and A923–A934 of proposed SAS No. 146, Quality Management for an Engagement Conducted in Accordance With Generally Accepted Auditing Standards.*

Application and Other Explanatory Material

~~.A1~~ *Proposed SAS No. 146 Quality Management for an Engagement Conducted in Accordance With Generally Accepted Auditing Standards addresses the specific responsibilities of the auditor regarding quality management at the engagement level for an audit of financial statements and the related responsibilities of the engagement partner. Information obtained from complying with the requirements of proposed SAS No. 146 Quality Management for an Engagement Conducted in Accordance With Generally Accepted Auditing Standards is relevant to this section. For example, in accordance with proposed SAS No. 146 Quality Management for an Engagement Conducted in Accordance With Generally Accepted Auditing Standards, the engagement partner is required to determine that sufficient and appropriate resources to perform the engagement have been assigned or made available to the engagement team, taking into account the nature and circumstances of the audit engagement. Such a determination is directly relevant when ascertaining the nature, timing, and extent of resources necessary to perform the engagement in the overall strategy, as required by paragraph .08 of this section.*

The Role and Timing of Planning (Ref: par. .01)

~~A1.A2~~ *The nature and extent of planning activities will vary according to the size and complexity of the entity, the key engagement team members' previous experience with the entity, and changes in circumstances that occur during the audit engagement. In planning the audit, the auditor may use project management techniques and tools. Proposed SAS No. 146 Quality Management for an Engagement Conducted in Accordance With Generally Accepted Auditing Standards^{fn 5} describes how such techniques and tools may support the engagement team in managing the quality of the engagement.*

^{fn 5} *Paragraphs A73–A74 of proposed SAS No. 146 Quality Management for an Engagement Conducted in Accordance With Generally Accepted Auditing Standards.*

[Subsequent footnotes are renumbered.]

[No amendment to paragraph .A2, renumbered as paragraph .A3.]

~~A3.A4~~ *The auditor may decide to discuss elements of planning with the entity's management to facilitate the conduct and management of the audit help the auditor manage and achieve quality at the engagement level (for example, to coordinate some of the planned audit procedures with the work of the entity's personnel). Although these discussions often occur, the overall audit strategy and the audit plan remain the auditor's responsibility. When discussing matters included in the overall audit strategy or audit plan, care is required in order not to compromise the effectiveness of the audit. For example, discussing the nature and timing of detailed audit procedures with management may compromise the effectiveness of the audit by making the audit*

procedures too predictable.

[No amendment to paragraphs .A4–.A5, renumbered as paragraphs .A5–.A6.]

Preliminary Engagement Activities (Ref: par. .06)

~~.A67~~ Performing the preliminary engagement activities, which are specified in paragraph .06, at the beginning of the current audit engagement assists the auditor in identifying and evaluating events or circumstances that may adversely affect the auditor’s ability to ~~plan and perform the audit engagement~~ **manage and achieve quality at the engagement level in accordance with proposed SAS No. 146 Quality Management for an Engagement Conducted in Accordance With Generally Accepted Auditing Standards.**

~~.A7A8~~ Performing these preliminary engagement activities enables the auditor to plan an audit engagement ~~for which to~~, for example

- ~~the auditor maintains~~ **maintain** the necessary independence and ability to perform the engagement.
- **determine that** the auditor has no issues with management integrity that may affect the auditor’s willingness to continue the engagement.
- **determine that there is** ~~the auditor has~~ no misunderstanding **between the auditor and** with the entity about the terms of the engagement.

~~.A8A9~~ The auditor’s consideration of client continuance and relevant ethical requirements, including independence, occurs throughout the audit engagement as conditions and changes in circumstances occur. Performing initial procedures on both client continuance and evaluation of relevant ethical requirements (including independence) at the beginning of the current audit engagement means that they are completed prior to the performance of other significant activities for the current audit engagement. For continuing audit engagements, such initial procedures often begin shortly after (or in connection with) the completion of the previous audit.

Planning Activities

The Overall Audit Strategy (Ref: par. .07–.08)

~~.A9A10~~ The process of establishing the overall audit strategy ~~assists the auditor to determine~~, subject to the completion of the auditor’s risk assessment procedures, **may include** such matters as the following:

- The **nature of** resources (**human, technological, or intellectual**) to ~~deploy~~ **be deployed** for specific audit areas, ~~such as for example, the use~~ **deployment** of ~~appropriately~~ experienced team members for high risk areas or the ~~involvement~~ **assignment** of specialists ~~on~~ **to address** complex matters
- The amount of resources to ~~allocate~~ **be allocated** to specific audit areas, ~~such as for example, the number of team members assigned to observe~~ **attend** the **physical** inventory count at ~~material~~ **multiple** locations, the extent of review of component auditors’ work in the case of group audits, or the audit budget (in hours) to allocate to high risk areas

- When these resources are to be deployed, such as whether at an interim audit stage or at key cut-off dates
- How such resources are managed, directed, and supervised, such as *or used, for example*, when team briefing and debriefing meetings are expected to be held, how the engagement partner and manager reviews are expected to take place (for example, on site or off site), and whether to complete engagement quality control reviews

~~.A11 Proposed SAS No. 146 Quality Management for an Engagement Conducted in Accordance With Generally Accepted Auditing Standards contains requirements and guidance on engagement resources and engagement performance (including direction and supervision of the members of the engagement team and the review of their work).~~

[No amendment to paragraphs .A10–.A17, renumbered as paragraphs .A12–.A19.]

Direction, Supervision, and Review (Ref: par. .11)

~~.A18A20 Proposed SAS No. 146 Quality Management for an Engagement Conducted in Accordance With Generally Accepted Auditing Standards addresses the engagement partner's responsibility for the~~ The nature, timing, and extent of the direction and supervision of engagement team members and review of their work.^{fn 10} vary, depending on many factors, including the following:

- ~~The size and complexity of the entity~~
- ~~The area of the audit~~
- ~~The assessed risks of material misstatement (for example, an increase in the assessed risk of material misstatement for a given area of the audit ordinarily requires a corresponding increase in the extent and timeliness of direction and supervision of engagement team members and a more detailed review of their work)~~
- ~~The capabilities and competence of the individual team members performing the audit work~~

~~Section 220 contains further guidance on the direction, supervision, and review of audit work.~~

~~^{fn 10} Paragraphs 29–31 of proposed SAS No. 146 Quality Management for an Engagement Conducted in Accordance With Generally Accepted Auditing Standards.~~

[Subsequent footnotes are renumbered.]

Considerations Specific to Smaller, Less Complex Entities Scalability

~~.A19A21~~ If an audit is carried out entirely by the engagement partner, questions of direction and supervision of engagement team members and review of their work do not arise. In such cases, the engagement partner, having personally conducted all aspects of the work, will be aware of all material issues. Forming an objective view on the appropriateness of the judgments made in the course of the audit can present practical problems when the same individual also performs the entire audit. If particularly complex or unusual issues are involved, and the audit is

performed by a sole practitioner, it may be desirable to consult with other suitably experienced auditors or the auditor’s professional body.

[No amendment to paragraphs .A20–.A21, renumbered as paragraphs .A22–.A23.]

Additional Considerations in Initial Audit Engagements (Ref: par. .13)

~~.A22~~**.A24** The purpose and objective of planning the audit are the same whether the audit is an initial or recurring engagement. However, for an initial audit, the auditor may need to expand the planning activities because the auditor does not ordinarily have the previous experience with the entity that is considered when planning recurring engagements. For an initial audit engagement, additional matters the auditor may consider in establishing the overall audit strategy and audit plan include the following:

- Arrangements to be made with the predecessor auditor (for example, to review the predecessor auditor’s working papers [see section 510, *Opening Balances — Initial Audit Engagements, Including Reaudit Engagements*])^{fn 8}
- Any major issues (including the application of accounting principles or auditing and reporting standards) discussed with management in connection with the initial selection as auditor, the communication of these matters to those charged with governance, and how these matters affect the overall audit strategy and audit plan
- The audit procedures necessary to obtain sufficient appropriate audit evidence regarding opening balances (see section 510)^{fn 9}
- Other procedures required *responses designed and implemented* by the ~~firm’s system of quality control~~ *firm* for initial audit engagements (for example, the firm’s system of quality control *management* may *include responses that* require the involvement of another partner or senior individual *with appropriate authority* to review the overall audit strategy prior to commencing significant audit procedures or to review reports prior to their issuance)

^{fn 8–9} [Footnotes renumbered as 11 and 12, and omitted for purposes of this exposure draft.]

Documentation (Ref: par. .14)

~~.A23~~**.A25** The documentation of the overall audit strategy is a record of the key decisions considered necessary to properly plan the audit *in managing quality at the engagement level* and *a means to* communicate significant issues to the engagement team. For example, the auditor may summarize the overall audit strategy in the form of a memorandum that contains key decisions regarding the overall scope, timing, and conduct of the audit.

~~.A26~~ *Documentation of the direction and supervision of engagement team members and the review of their work in accordance with proposed SAS No. 146 Quality Management for an Engagement Conducted in Accordance With Generally Accepted Auditing Standards may also provide a record of significant changes to the planned nature, timing, and extent of the direction, supervision, and review.*

[No amendment to paragraphs .A24–.A26, renumbered as paragraphs .A27–.A29.]

Appendix — Considerations in Establishing the Overall Audit Strategy *Managing Quality at the Engagement Level (Ref: par. .07–.08 and .A9–.A12)*

~~A27A30~~

This appendix provides examples of matters the auditor may consider in ~~establishing the overall audit strategy~~ **managing quality at the engagement level**. Many of these matters also will influence the auditor's **overall audit strategy and** detailed audit plan. The examples provided cover a broad range of matters applicable to many engagements. Although some of the following matters may be required by other AU-C sections, not all matters are relevant to every audit engagement, and the list is not necessarily complete.

...

Nature, Timing, and Extent of Resources

The following examples illustrate the nature, timing, and extent of resources:

- The ~~selection~~ **human, technological, and intellectual resources assigned or made available to the engagement (for example, assignment of the engagement team (including, when necessary, the engagement quality control reviewer [see section 220, *Quality Control for an Engagement Conducted in Accordance With Generally Accepted Auditing Standards*]) and the assignment of audit work to the team members, including the assignment of appropriately experienced team members to areas in which there may be higher risks of material misstatement**
- Engagement budgeting, including considering the appropriate amount of time to set aside for areas in which there may be higher risks of material misstatement

[No further amendment to AU-C section 300.]

6. This amendment is effective for audits of financial statements for periods beginning on or after December 15, 2025.

AU-C Section 600, *Special Considerations—Audits of Group Financial Statements (Including the Work of Component Auditors)*

Introduction

Scope of This Section

[No amendment to paragraphs .01–.04.]

.05 In accordance with ~~section 220,~~ **proposed Statement on Auditing Standards (SAS) No. 146, *Quality Control Management for an Engagement Conducted in Accordance With Generally Accepted Auditing Standards***, the group engagement partner is required to ~~be satisfied~~ **determine** that those performing the group audit engagement, including component auditors, collectively possess the appropriate competence and capabilities, **including sufficient time**.^{fn 1} The group

engagement partner also is responsible for the direction ~~and~~; supervision *of members of the group engagement team*, and ~~performance of the group audit engagement review of their work.~~^{fn2} In this section, requirements to be undertaken by the group engagement partner are addressed to the group engagement partner. When the group engagement team may assist the group engagement partner in fulfilling a requirement, the requirement is addressed to the group engagement team. When it may be appropriate in the circumstances for the firm to fulfill a requirement, the requirement is addressed to the auditor of the group financial statements.

^{fn 1} Paragraphs 1625–26 of section 220, *proposed Statement on Auditing Standards (SAS) No. 146, Quality Control Management for an Engagement Conducted in Accordance With Generally Accepted Auditing Standards*.

^{fn 2} ~~Paragraphs 29–31 of proposed SAS No. 146 statement on Auditing Standards Quality Management for an Engagement Conducted in Accordance With Generally Accepted Auditing Standards.~~

[Subsequent footnotes are renumbered.]

[No further amendment to AU-C section 600.]

7. This amendment is effective for audits of group financial statements for periods beginning on or after December 15, 2025.

AU-C Section 620, *Using the Work of an Auditor’s Specialist*

[No amendment to paragraphs .01–.07.]

.08 The nature, timing, and extent of the auditor’s procedures with respect to the requirements in paragraphs .09–.13 will vary depending on the circumstances. In determining the nature, timing, and extent of those procedures, the auditor should consider matters including (Ref: par. .A11)

- a. the nature of the matter to which the work of the auditor’s specialist relates;
- b. the risks of material misstatement in the matter to which the work of the auditor’s specialist relates;
- c. the significance of the work of the auditor’s specialist in the context of the audit;
- d. the auditor’s knowledge of, and experience with, previous work performed by the auditor’s specialist; and
- e. whether the auditor’s specialist is subject to the auditor’s firm’s **system of quality management control policies and procedures**. (Ref: par. .A12–.A14)

[No amendment to paragraphs .09–.A6.]

.A7 If the preparation of the financial statements involves the use of expertise in a field

other than accounting, the auditor, who is skilled in accounting and auditing, may not possess the necessary expertise to audit those financial statements. The engagement partner is required by section 220 ~~proposed-Statement on Auditing Standards (SAS) No. 146, Quality Management for an Engagement Conducted in Accordance With Generally Accepted Auditing Standards,~~ to be satisfied ~~to~~ **determine** that the engagement team and any external auditor's specialists who are not part of the engagement team, collectively, have the appropriate competence and capabilities, **including sufficient time**, to perform the audit engagement.^{fn 6} Further, the auditor is required by section 300 to ascertain the nature, timing, and extent of resources necessary to perform the engagement.^{fn 7} The auditor's determination of whether to use the work of an auditor's specialist, and, if so, when and to what extent, assists the auditor in meeting these requirements. As the audit progresses or as circumstances change, the auditor may need to revise earlier decisions about using the work of an auditor's specialist.

^{fn 6} Paragraph 4626 of section 220 ~~proposed-Statement on Auditing Standards (SAS) No. 146, Quality Management for an Engagement Conducted in Accordance With Generally Accepted Auditing Standards.~~

^{fn 7} [Footnote omitted for purposes of this exposure draft.]

[No amendment to paragraphs .A8–.A10.]

.A11 The following factors may suggest the need for different or more extensive procedures than would otherwise be the case:

- The work of the auditor's specialist relates to a significant finding or issue that involves subjective and complex judgments.
- The auditor has not previously used the work of the auditor's specialist and has no prior knowledge of that specialist's competence, capabilities, and objectivity.
- The auditor's specialist is performing procedures that are integral to the audit rather than being consulted to provide advice on an individual matter.
- The specialist is an auditor's external specialist and is not, therefore, subject to the firm's **system of quality management** ~~control policies and procedures~~.

The Auditor's Firm's System of Quality Control Policies and Procedures Management (Ref: par. .08e)

.A12 An auditor's internal specialist may be a partner or staff, including temporary staff (**that is, personnel**), of the auditor's firm and, therefore, subject to the **system of quality control policies and procedures management** of that firm in accordance with QC section 10, ~~proposed Statement on Quality Management Standards (SOMS) No. 1, A Firm's System of Quality Control Management.~~^{fn 10} An auditor's internal specialist also may be a partner or staff, including temporary staff, of a network firm, **and is subject to the firm's policies or procedures for network requirements and network services in accordance with proposed Statement on Quality Management Standards A Firm's System of Quality Management SOMS No. 1. In**

some instances, the auditor’s internal specialist of a network firm may be subject to which may share common quality control management policies and or procedures with as the auditor’s firm, given that they are part of the same network.

^{fn 10} Paragraph 1317 of *proposed Statement on Quality Management Standards (SQMS) No. 1, A Firm’s System of Quality Management.*

.A13 ~~In accordance with As described in section 220~~ *proposed SAS No. 146 Quality Management for an Engagement Conducted in Accordance With Generally Accepted Auditing Standards, quality management at the engagement teams are entitled to rely on the firm’s system of quality control unless the engagement partner determines that it is inappropriate to do so based on information provided by the firm or other parties.^{fn 11} *The extent of that reliance will vary with the circumstances and may affect the nature, timing, and extent of the auditor’s level is supported by the firm’s system of quality management and informed by the specific nature and circumstances of the audit engagement.*^{fn 12} *For example, the auditor may be able to depend on the firm’s related policies or procedures with respect to such matters as the following:**

- Competence and capabilities through recruitment and training programs.
- Objectivity. The auditor’s internal specialists are subject to relevant ethical requirements, including those ~~pertain~~ *relating* to independence.
- Agreement with the auditor’s specialist.
- The auditor’s evaluation of the adequacy of the work of the auditor’s specialist. For example, the firm’s training programs may provide the auditor’s internal specialists with an appropriate understanding of the interrelationship of their expertise with the audit process. Reliance on such training ~~and other firm processes, such as protocols for scoping the work of the auditor’s internal specialists,~~ may affect the nature, timing, and extent of the auditor’s procedures to evaluate the adequacy of the work of the auditor’s specialist.
- Adherence to regulatory and legal requirements through monitoring processes.

Such reliance Matters that the auditor may take into account when determining whether to depend on the firm’s policies or procedures are described in ~~proposed SAS No. 146 Quality Management for an Engagement Conducted in Accordance With Generally Accepted Auditing Standards.~~^{fn 13} *Depending on the firm’s policies or procedures does not reduce the auditor’s responsibility to meet the requirements of this section.*

^{fn 11} Paragraph .05 of section 220:

^{fn 12} Paragraph A4 of *proposed SAS No. 146 Quality Management for an Engagement Conducted in Accordance With Generally Accepted Auditing Standards.*

~~*^{fn 13} Paragraphs 04b and A10 of proposed SAS No. 146 Quality Management for an Engagement Conducted in Accordance With Generally Accepted Auditing Standards.*~~

~~**.A14** *Proposed SOMS No. 1 statement on Quality Management Standards A Firm's System of Quality Management requires the firm to address the use of resources from a service provider, which includes the use of an external specialist.* ^{fn14} An auditor's external specialist is not a member of the engagement team and is not subject to quality control policies and procedures in accordance with QC section 10 *the firm's policies or procedures under its system of quality management.* ^{fn 15} *Furthermore, the firm's policies or procedures for relevant ethical requirements may include policies or procedures that apply to the auditor's external specialist.* ^{fn 12 16}~~

~~*^{fn 14} Paragraph 33 of proposed SOMS No. 1 statement on Quality Management Standards A Firm's System of Quality Management.*~~

~~*^{fn 15} Paragraph 17 of proposed SOMS No. 1 statement on Quality Management Standards A Firm's System of Quality Management.*~~

~~*^{fn 12/16} Paragraph 13.30b of QC section 10 proposed SOMS No. 1 statement on Quality Management Standards A Firm's System of Quality Management.*~~

[Subsequent footnotes are renumbered.]

[No proposed amendment to paragraph .A15.]

.A16 Information regarding the competence, capabilities, and objectivity of an auditor's specialist may come from a variety of sources, such as the following:

- Personal experience with previous work of that specialist
- Discussions with that specialist
- Discussions with other auditors or others who are familiar with that specialist's work
- Knowledge of that specialist's qualifications, membership in a professional body or industry association, license to practice, or other forms of external recognition
- Published papers or books written by that specialist
- The **system of quality management** ~~control policies and procedures~~ of the auditor's firm and such other procedures the auditor considers necessary in the circumstances (see paragraphs .A12–.A13).

[No amendment to paragraphs .A17–.A28.]

.A29 When no written agreement exists between the auditor and the auditor's specialist, evidence of the agreement may be included in, for example

- planning memoranda or related working papers, such as the audit program.
- the policies ~~and or~~ procedures of the auditor’s firm’s ***system of quality management***. In the case of an auditor’s internal specialist, the ~~established policies and procedures to which the auditor’s specialist is subject~~ ***firm’s system of quality management*** may include ~~particular~~ policies ~~and or~~ procedures regarding the work of the auditor’s specialist. The extent of documentation in the auditor’s working papers depends on the nature of such policies ~~and or~~ procedures. For example, no documentation may be required in the auditor’s working papers if the auditor’s firm has detailed protocols covering the circumstances in which the work of such an auditor’s specialist is used.

[No further amendment to AU-C section 620.]

8. This amendment is effective for audits of financial statements for periods beginning on or after December 15, 2025.

AU-C section 930, *Interim Financial Information*

[No amendment to paragraphs .01–.A59.]

.A60 When an engagement quality ~~control~~ review is performed, ~~section 220, ***proposed Statement on Auditing Standards (SAS) No. 146, Quality Control Management*** for an Engagement Conducted in Accordance With Generally Accepted Auditing Standards, requires that the ***engagement partner not date the auditor’s report not be released prior to*** ***until*** the completion of the engagement quality ~~control~~ review.^{fn 27}~~

^{fn 27} Paragraph 21.36d of section 220 ~~***proposed Statement on Auditing Standards No. 146, Quality Control Management*** for an Engagement Conducted in Accordance With Generally Accepted Auditing Standards.~~

[No further amendment to AU-C section 930.]

9. This amendment is effective for reviews of interim financial information for interim periods of fiscal years beginning on or after December 15, 2025.

Amendment to SAS No. 130, *An Audit of Internal Control Over Financial Reporting That Is Integrated With an Audit of Financial Statements*, as Amended

(***Boldface italics*** denotes new language. Deleted text is in ~~strike through~~.)

AU-C Section 940, *An Audit of Internal Control Over Financial Reporting That Is Integrated With an Audit of Financial Statements*

[No amendment to paragraphs .01–.A116.]

.A117 ~~Section 220, *Proposed Statement on Auditing Standards (SAS) No. 146, Quality Control Management for an Engagement Conducted in Accordance With Generally Accepted Auditing Standards*~~, requires that, on or before the date of the auditor’s report, the engagement partner **determine**, through a review of the audit documentation and discussion with the engagement team, ~~be satisfied~~ that sufficient appropriate audit evidence has been obtained to support the conclusions reached and for the auditor’s report to be issued.^{fn 25} When an engagement quality control review is performed, ~~section 220 *proposed SAS No. 146 statement on Auditing Standards Quality Management for an Engagement Conducted in Accordance With Generally Accepted Auditing Standards*~~ requires that the **engagement partner not date the** auditor’s report ~~not be released prior to~~ **until** the completion of the engagement quality control review.^{fn 26}

^{fn 25} See paragraph ~~Paragraph 1932~~ of section 220, ~~*proposed SAS No. 146, Quality Control Management for an Engagement Conducted in Accordance With Generally Accepted Auditing Standards*~~, for further discussion.

^{fn 26} Paragraph ~~2136d~~ of section 220 ~~*proposed SAS No. 146 Quality Control Management for an Engagement Conducted in Accordance With Generally Accepted Auditing Standards*~~.

[No further amendment to AU-C section 940.]

10. This amendment is effective for integrated audits for periods beginning on or after December 15, 2025.

Amendments to Various Sections in SAS No. 134, *Auditor Reporting and Amendments, Including Amendments Addressing Disclosures in the Audit of Financial Statements*, as Amended

(*Boldface italics* denotes new language. Deleted text is in ~~strike through~~.)

AU-C Section 700, *Forming an Opinion and Reporting on Financial Statements*

[No amendment to paragraphs .01–.A38.]

.A39 Relevant ethical requirements may exist in several different sources, such as ethical codes and additional rules and requirements within law and regulation. When independence and other relevant ethical requirements are contained in a limited number of sources, the auditor may

choose to name the relevant sources (for example, the AICPA Code of Professional Conduct, when applicable; the rule or applicable regulation; or *Government Auditing Standards* promulgated by the Comptroller General of the United States) or may refer to a term that appropriately describes those sources. Relevant ethical requirements, including those ~~pertaining~~ **relating** to independence, in a group audit situation may be complex. Section 600, *Special Considerations — Audits of Group Financial Statements (Including the Work of Component Auditors)*,^{fn 21} provides guidance for auditors in performing work on the financial information of a component for a group audit, including those situations in which the component auditor does not meet the independence requirements that are relevant to the group audit.

^{fn 21} [Footnote omitted for purposes of this exposure draft.]

[No amendment to paragraphs .A40–.A53.]

.A54 ~~Section 220, Quality Control Management~~ ***Proposed Statement on Auditing Standards (SAS) No. 146, Section 220, Quality Control Management*** for an Engagement Conducted in Accordance With Generally Accepted Auditing Standards, requires ***the following with regard to dating the auditor’s report:***

- ~~that~~ ***On or before the date of the auditor’s report, the engagement partner, through a review of the audit documentation and discussion with the engagement team, is required to be satisfied that sufficient appropriate audit evidence has been obtained to support the conclusions reached and for the auditor’s report to be issued.***^{fn 26}
- ***Prior to dating the auditor’s report, the engagement partner is required to review the financial statements and the auditor’s report, including, if applicable, the description of the key audit matters and related audit documentation, to determine that the report to be issued will be appropriate in the circumstances.***^{fn 27}
- When an engagement quality ~~control~~ review is performed, ~~section 220~~ ***the engagement partner is precluded from dating-releasing the auditor’s report not be released prior to until the completion of the engagement quality ~~control~~ review.***^{fn 278}

^{fn 26} See paragraph ~~Paragraph 1932~~ of ~~section 220, proposed-SAS No. 146, Quality Control Management~~ for an Engagement Conducted in Accordance With Generally Accepted Auditing Standards, ~~for further discussion.~~

^{fn 27} ~~Paragraph 33 of proposed-SAS No. 146~~ ***Quality Management for an Engagement Conducted in Accordance With Generally Accepted Auditing Standards.***

^{fn 278} Paragraph ~~2436d~~ of ~~section 220, proposed-SAS No. 146~~ ***Quality Control Management for an Engagement Conducted in Accordance With Generally Accepted Auditing Standards.***

[No further amendment to AU-C section 700.]

11. This amendment is effective for audits of financial statements for periods beginning on or after December 15, 2025.

AU-C Section 701, *Communicating Key Audit Matters in the Independent Auditor’s Report*

[No amendment to paragraphs .01–.A12.]

.A13 Certain AU-C sections, such as the following, require specific communications with those charged with governance and others that may relate to areas of significant auditor attention:

- a. Section 260, *The Auditor’s Communication With Those Charged With Governance*, requires the auditor to communicate significant difficulties, if any, encountered during the audit with those charged with governance.^{fn 7} For example, there may be potential difficulties relating to the following:
 - i. *Related party transactions*. In particular, there may be limitations on the auditor’s ability to obtain audit evidence that all other aspects of a related party transaction (other than price) are equivalent to those of a similar arm’s-length transaction.^{fn 8}
 - ii. *Limitations on the group audit*. For example, the group engagement team’s access to information may be restricted.^{fn 9}

^{fns 7–9} [Footnotes omitted for purposes of this exposure draft.]

- b. ~~Section 220, *Proposed-Statement on Auditing Standards No. 146, Quality Control Management for an Engagement Conducted in Accordance With Generally Accepted Auditing Standards*, establishes requirements for the engagement partner in relation to undertaking appropriate consultation on difficult or contentious matters and matters on which the firm’s policies or procedures require consultation and other matters that in the engagement partner’s professional judgment, require consultation.~~^{fn 10} For example, the auditor may have consulted with others within the firm or outside the firm on a significant technical matter, which may be an indicator that it is a key audit matter. The engagement partner is also required to discuss, among other things, significant matters *and significant judgments* arising during the audit engagement with the engagement quality ~~control~~ reviewer.

^{fn 10} Paragraph 2035 of section 220, ~~proposed SAS No. 146, *Quality Control Management for an Engagement Conducted in Accordance With Generally Accepted Auditing Standards*.~~

[No amendment to paragraphs .A14–.A59.]

Communication With Those Charged With Governance (Ref: par. .16)

.A60 ~~*Proposed SAS No. 146 Quality Management for an Engagement Conducted in Accordance With Generally Accepted Auditing Standards, requires the engagement partner, prior to dating the auditor’s report, to review the financial statements and the auditor’s report, including, if applicable, the description of the key audit matters and related audit documentation, to determine that the report to be issued will be*~~

*appropriate in the circumstances.*¹⁹

¹⁹ Paragraph 33 of ~~proposed SAS No. 146~~ *Quality Management for an Engagement Conducted in Accordance With Generally Accepted Auditing Standards*.

[No amendment to paragraph .A60, renumbered as paragraph .A61.]

~~.A61~~ The requirement in paragraph .16b to communicate with those charged with governance when the auditor has determined that there are no key audit matters to communicate in the auditor’s report may provide an opportunity for the auditor to have further discussion with others who are familiar with the audit and the significant matters that may have arisen (including the engagement quality ~~control~~ reviewer, when one has been appointed). These discussions may cause the auditor to reevaluate the auditor’s determination that there are no key audit matters.

[No amendment to paragraph .A62, renumbered as .A63.]

12. This amendment is effective for audits of financial statements for periods beginning on or after December 15, 2025.

Amendment to SAS No. 136, Forming an Opinion and Reporting on Financial Statements of Employee Benefit Plans Subject to ERISA, as Amended

(*Boldface italics* denotes new language. Deleted text is in ~~strike through~~.)

AU-C Section 703, Forming an Opinion and Reporting on Financial Statements of Employee Benefit Plans Subject to ERISA

[No amendment to paragraphs .01–.A118.]

Date of the Auditor’s Report (Ref: par. .82 and .126)

~~A119. Proposed SAS No. 146, Section 220, Quality Control Management~~ *for an Engagement Conducted in Accordance With Generally Accepted Auditing Standards, requires the following with regard to dating the auditor’s report:*

- ~~that,~~ *On or before the date of the auditor’s report, the engagement partner, through a review of the audit documentation and discussion with the engagement team, is required to be satisfied that sufficient appropriate audit evidence has been obtained to support the conclusions reached and for the auditor’s report to be issued.*^{fn44}
- *Prior to dating the auditor’s report, the engagement partner is required to review the financial statements and the auditor’s report, including, if applicable, the description of the key audit matters and related audit documentation, to determine that the report to be issued will be appropriate in the circumstances.*^{fn45}

- When an engagement quality control review is performed, ~~section 220~~ the **engagement partner is precluded from ~~dating-releasing the~~ auditor’s report not be released prior to until** the completion of the engagement quality control review. ^{fn 4546}

^{fn 44} See ~~paragraph~~ **Paragraph 1932** of section 220, ~~proposed SAS No. 146, Quality Control Management for an Engagement Conducted in Accordance With Generally Accepted Auditing Standards, for further discussion.~~

^{fn 45} ~~Paragraph 33 of SAS No. 146~~ **Quality Control Management for an Engagement Conducted in Accordance With Generally Accepted Auditing Standards, for further discussion.**

^{fn 4546} Paragraph ~~2136d~~ of section 220 ~~proposed SAS no. 146~~ **Quality Control Management for an Engagement Conducted in Accordance With Generally Accepted Auditing Standards.**

[No further amendment to AU-C section 703.]

13. This amendment is effective for audits of ERISA plan financial statements for periods beginning on or after December 15, 2025.

Amendment to SAS No. 137, The Auditor’s Responsibilities Relating to Other Information Included in Annual Reports, as Amended

(***Boldface italics*** denotes new language. Deleted text is in ~~strike through~~.)

AU-C section 720, Other Information Included in Annual Reports

[No amendment to paragraphs .01–.A26.]

.A27 In accordance with ~~section 220, proposed Statement on Auditing Standards No. 146, Quality Control Management for an Engagement Performed in Accordance With Generally Accepted Auditing Standards,~~ ^{fn 8} the engagement partner is required to take responsibility for the direction, ~~and supervision, and performance of the audit engagement of the members of the engagement team and the review of their work, and determine that the nature, timing, and extent of direction, supervision, and review is planned and performed~~ in compliance with ***the firm’s policies or procedures***, professional standards, and applicable legal and regulatory requirements. ^{fn 8} In the context of this section, factors that may be considered when determining the appropriate engagement team members to address the requirements of paragraphs .16–.17 of this section include the following:

- The relative experience of engagement team members

- Whether the engagement team members have the relevant knowledge obtained in the audit to identify inconsistencies between the other information and that knowledge
- The degree of judgment involved in addressing the requirements of paragraphs .16–.17 of this section, for example, performing procedures to evaluate the consistency of amounts in the other information that are intended to be the same as amounts in the financial statements may be carried out by less experienced engagement team members
- Whether, in the case of a group audit, it is necessary to make inquiries of a component auditor in addressing the other information related to that component

^{fn 8} Paragraphs ~~17a-29-30~~ of section ~~220~~ **proposed SAS no. 146, Quality Control Management for an Engagement Performed in Accordance With Generally Accepted Auditing Standards.**

[No further amendment to AU-C section 720.]

14. This amendment is effective for audits of financial statements for periods beginning on or after December 15, 2025.

Amendment to SAS No. 142, *Audit Evidence*

Appendix B — Amendments to Various Sections in Statement on Auditing Standards No. 122, *Statements on Auditing Standards: Clarification and Recodification*, as Amended

.A68

...

AU-C Section 200, Overall Objectives of the Independent Auditor and the Conduct of an Audit in Accordance With Generally Accepted Auditing Standards

.A27 Unconscious or conscious auditor biases may affect the auditor’s professional skepticism and professional judgment, including, for example, in the design and performance of audit procedures or the evaluation of audit evidence. Examples of unconscious auditor biases are provided in paragraph A35 of ~~proposed~~ Statement on Auditing Standards **No. 146, Quality Management of an Audit Conducted in Accordance With Generally Accepted Auditing Standards.** ~~that may impede the maintenance of professional skepticism and, therefore, the reasonableness of the professional judgments made by the auditor in complying with the requirements of this section, may include the following:~~

- ~~Availability bias, which is a tendency to place more weight on events or experiences that immediately come to mind or are readily available than on those that are not~~
- ~~Confirmation bias, which is a tendency to place more weight on information that corroborates an existing belief than information that contradicts or casts doubt on that belief~~
- ~~Overconfidence bias, which is a tendency to overestimate one's own ability to make accurate assessments of risk or other judgments or decisions~~
- ~~Anchoring bias, which is a tendency to use an initial piece of information as an anchor against which subsequent information is inadequately assessed~~
- ~~Automation bias, which is a tendency to favor output generated from automated systems, even when human reasoning or contradictory information raises questions about whether such output is reliable or fit for purpose~~

[Paragraphs .A27–.A86 have been renumbered.]

15. This amendment is effective for audits of financial statements for periods beginning on or after December 15, 2025.

Amendment to Statement on Standards for Attestation Engagements No. 18, *Attestation Standards: Clarification and Recodification*, as Amended, Section 105, *Concepts Common to All Attestation Engagements*

(*Boldface italics* denotes new language. Deleted text is in ~~strike through~~.)

AT-C Section 105, *Concepts Common to All Attestation Engagements*

[No amendment to paragraphs .01–.05.]

Relationship of Attestation Standards to Quality Control Standards

~~.06~~ Quality ~~control~~ **management** systems, policies, and procedures are the responsibility of the firm in conducting its attestation practice. Under QC section 10 ~~proposed Statement on Quality Management Standards No. 1, A Firm's System of Quality Control Management~~, the firm has an obligation to ~~establish~~ **design, implement, and maintain** ~~operate~~ a system of quality ~~control~~ **management** to provide it **that provides the firm** with reasonable assurance that ^{fn5} (Ref: par. ~~.A4–.A6~~)

- a. the firm and its personnel ~~comply~~ **fulfill their responsibilities in accordance** with professional standards and applicable legal and regulatory requirements **and conduct attestation engagements in accordance with such standards and requirements**, and

b. practitioners' reports issued by the firm are appropriate in the circumstances.

^{in 5} Paragraph 1220 of QC section 10, ~~proposed~~ *Statement on Quality Management Standards No. 1, A Firm's System of Quality Control Management* (AICPA, *Professional Standards*).

.07 Attestation standards relate to the conduct of individual attestation engagements; quality ~~control~~ *management* standards relate to the conduct of a firm's attestation practice as a whole. Thus, attestation standards and quality ~~control~~ *management* standards are related, and the quality ~~control~~ *management* policies ~~and~~ *or* procedures that a ~~the~~ firm ~~adopts~~ *establishes* may affect both the conduct of individual attestation engagements and the conduct of ~~a~~ *the* firm's attestation practice as a whole. However, deficiencies in or instances of noncompliance with ~~a~~ *the* firm's quality ~~control~~ *management* policies and procedures do not, in and of themselves, indicate that a particular engagement was not ~~performed~~ *conducted* in accordance with the attestation standards.

[No further amendment to AT-C section 105.]

16. This amendment is effective for practitioners' reports dated on or after December 15, 2025.

QM Section Appendix—Substantial Differences Between the ISQMs and the SQMSs

Comparison of Section 10, *A Firm's System of Quality Management*, and International Standard on Quality Management 1, *Quality Management for Firms that Perform Audits and Reviews of Financial Statements, and Other Assurance and Related Services Engagements*

This analysis was prepared by the AICPA Audit and Attest Standards staff to highlight substantive differences between the International Standards on Quality Management (ISQM) and the Statements on Quality Management Standards (SQMS) codified in QM section 10-20, and the rationale therefore. This analysis is not authoritative and is prepared for informational purposes only. It has not been acted on or reviewed by the Auditing Standards Board (ASB).

This analysis compares the ISQMs included in the [2022] edition of the *Handbook of International Quality Control, Auditing, Review, Other Assurance, and Related Services Pronouncements*, to the AICPA's *Professional Standards* as of January [2023]. References to SQMSs are made to the relevant QM sections. This analysis describes the differences in terms of

- a. differences in wording,
- b. requirements in the ISQMs not in the QM sections,
- c. requirements in the QM sections not in the ISQMs and,
- d. differences between requirements.

General

In converging with the ISQMs, the ASB has made various changes to the wording of the ISQMs throughout the SQMSs. Such changes have been made to use terms applicable in the United States and to make the SQMSs easier to read and apply in the United States. The ASB believes that such changes do not create differences between the application of the ISQMs and the application of the SQMSs. Selected changes are described in the analysis that follows.

ISQM 1, *Quality Management for Firms that Perform Audits and Reviews of Financial Statements, and Other Assurance and Related Services Engagements*, Compared to QM Section 10, *A Firm’s System of Quality Management*

Requirements in ISQM 1 Not in Section 10

Paragraph 35 of ISQM 1 contains requirements relating to audits of listed entities. Such requirements are not applicable to audits of nonissuers in the United States and, accordingly, such requirements are not included in GAAS.

Paragraph 39(b) of ISQM 1 prohibits the engagement team members or the engagement quality reviewer from performing any inspection of that engagement. Section 10 does not include this prohibition. The ASB concluded that it was not necessary to change existing practice because in the United States, the peer review process provides a safeguard and provides evidence whether the monitoring procedures are effective.

ISQM 2, *Engagement Quality Reviews*, Compared to Section 20, *Engagement Quality Reviews*

Requirements in ISQM 2 Not in Section 20

Paragraph 19 of ISQM 2 requires a cooling-off period of two years before the engagement partner can assume the role of engagement quality reviewer. Section 20 does not include this requirement. The AICPA Code of Professional Conduct does not require engagement partner rotation, and ASB believes it would be inconsistent in the US to require a cooling-off period for engagement quality reviewers but not engagement partner rotation.

Requirements in ISQM 2 Revised in Section 20

Paragraph 24(b) of ISQM 2 precludes the engagement partner from *dating* the engagement report before receiving notification that the engagement quality review is complete. Paragraph .24b of section 20 precludes the engagement partner from *releasing* the engagement report before receiving notification that the engagement quality review is complete. The ASB believes that the flexibility of using the report release date provides greater benefit than the logistical cost of restricting the time available for completing the engagement quality review. As noted in the application material to section 20, when the engagement quality review results in additional procedures having to be performed, the date of the report would be changed.

AU-C Section Appendix B – *Substantive Differences Between the International Standards on Auditing and Generally Accepted Auditing Standards*

ISA 220 (Revised), *Quality Control for an Audit of Financial Statements*, Compared to Section 220, *Quality Control for an Engagement Conducted in Accordance With Generally Accepted Auditing Standards*

Requirements in the ISAs Not in GAAS

Paragraph 21 of ISA 220 contains requirements relating to audits of listed entities. Such requirements are not applicable to audits of nonissuers in the United States and, accordingly, such requirements are not included in GAAS.

Differences Between Requirements

Paragraph .36(d) of section 220 requires that when an engagement quality review is performed, the engagement quality review be completed before the engagement partner releases the auditor's report. Paragraph 36(d) of ISA 220 requires that the quality review be completed before the engagement partner dates the auditor's report. The ASB believes that the flexibility of using the report release date provides greater benefit than the logistical cost of restricting the time available for completing the engagement quality review. As noted in the application material to section 220, when the engagement quality review results in additional procedures being performed, the date of the report would be changed.



**~~INTERNATIONAL STANDARD STATEMENT ON QUALITY~~
MANAGEMENT NO. 1, *A Firm's System of Quality Management*
Quality Management for Firms That Perform Audits or Reviews
of Financial Statements, or Other Assurance or Related Services
*Engagements***

~~(Effective as of December 15, 2022)~~

CONTENTS

	Paragraph
Introduction	
Scope of This ISQM<u>SQMS</u>	1-56
The Firm's System of Quality Management	6-11 <u>7-12</u>
Authority of this ISQM <u>SQMS</u>	4 <u>13</u>
Effective Date	4 <u>14</u>
Objective	14-15 <u>16</u>
Definitions	4 <u>17</u>
Requirements	
Applying, and Complying with, Relevant Requirements	17-18 <u>19</u>
System of Quality Management	19-22 <u>20-23</u>
The Firm's Risk Assessment Process	23-27 <u>24-28</u>
Governance and Leadership	28 <u>29</u>
Relevant Ethical Requirements	29 <u>30</u>
Acceptance and Continuance of Client Relationships and Specific Engagements	30 <u>31</u>
Engagement Performance	31 <u>32</u>
Resources	32-33

Information and Communication	33 <u>34</u>
Specified Responses	34 <u>35</u>
Monitoring and Remediation Process	35-47 <u>36-48</u>
Network Requirements or Network Services	48-52 <u>49-53</u>
Evaluating the System of Quality Management	53-56 <u>54-57</u>
Documentation	57-60 <u>58-61</u>
Application and Other Explanatory Material	
Scope of this ISQM <u>SQMS</u>	A1- A2
The Firm's System of Quality Management	A3-A5 <u>A2-A4</u>
Authority of this ISQM <u>SQMS</u>	A6-A9 <u>A5-A8</u>
Definitions	A10 -A28
Applying, and Complying with, Relevant Requirements	A29
System of Quality Management	A30- A38 <u>A39</u>
The Firm's Risk Assessment Process	A39-A54 <u>A40-A56</u>
Governance and Leadership	A55-A61 <u>A57-A63</u>
Relevant Ethical Requirements	A62-A66 <u>A64-A68</u>
Acceptance and Continuance of Client Relationships and Specific Engagements	A67-A74 <u>A69- A78</u>
Engagement Performance	A75-A85 <u>A79-A89</u>
Resources	A86-A108 <u>A90-A115</u>
Information and Communication	A109-A115 <u>A116-A123</u>
Specified Responses	A116-A137 <u>A124-A147</u>
Monitoring and Remediation Process	A138-A174 <u>A148-A190</u>
Network Requirements or Network Services	A175-A186 <u>A191-A205</u>
Evaluating the System of Quality Management	A187-A204 <u>A206-A223</u>
Documentation	A202-A206 <u>A224-A228</u>

Introduction	Explanation of differences
Scope of This ISQM <u>Statement on Quality Management Standards</u>	
<p>1. This International Standard <u>Statement</u> on Quality Management <u>Standards</u> (ISQM <u>SQMS</u>) deals with a firm’s responsibilities to design, implement, and operate a system of quality management for audits or reviews of financial statements, or other assurance or related services engagements <u>its accounting and auditing practice</u>.</p>	Specific to U.S.
<p>2. Engagement quality reviews form part of the firm’s system of quality management and:</p>	
<p>a. this ISQM deals with <u>SQMS addresses</u> the firm’s responsibility to establish policies or procedures addressing engagements that are required to be subject to engagement quality reviews.</p>	ASB preferred wording
<p>b. <u>SQMS No. 2, Engagement Quality Reviews</u>, ISQM-2[†] deals with the appointment and eligibility of the engagement quality reviewer, and the performance and documentation of the engagement quality review.</p>	

[†] ~~ISQM-2, Engagement Quality Reviews~~

<p>3. Other pronouncements of the International Auditing and Assurance professional standards Board (IAASB): a. Are premised on the basis that the firm is subject to the ISQMs or to national requirements that are at least as demanding;² and b. include requirements for engagement partners and other engagement team members regarding quality management at the engagement level. For example, ISA 220 (Revised) <u>Statement on Auditing Standards (SAS) No. 146, <i>Quality Management for an Engagement Conducted in Accordance With Generally Accepted Auditing Standards</i></u>, deals with the specific responsibilities of the auditor regarding quality management at the engagement level for an audit of financial statements and the related responsibilities of the engagement partner. <u>Other professional standards, including AT-C section 105, <i>Concepts Common to All Attestation Engagements</i></u>,[‡] and AR-C section 60, <i>General Principles for Engagements Performed in Accordance With Statements on Standards for Accounting and Review Services</i>,[‡] <u>also establish requirements for the engagement partner for the management of quality at the engagement level.</u></p>	<p>Specific to U.S.</p>
<p>4. <u>This SQMS is to be read in conjunction with the AICPA Code of Professional Conduct (AICPA code) and other relevant ethical requirements. Law, regulation, or relevant ethical requirements may establish responsibilities for the firm’s management of quality beyond those described in this SQMS.</u> (Ref: par. A1)</p>	<p>Specific to U.S.</p>
<p>4. This ISQM is to be read in conjunction with relevant ethical requirements. Law, regulation or relevant ethical requirements may establish responsibilities for the firm’s management of quality beyond those described in this ISQM. (Ref: par. A2)</p>	
<p>5. <u>This SQMS applies to audit and attestation engagements performed by a firm in accordance with <i>Government Auditing Standards</i>. This SQMS does not apply to government audit organizations. Instead, those government audit organizations are subject to the quality control and assurance requirements of <i>Government Auditing Standards</i>.</u></p>	<p>Specific to U.S.</p>
<p>6. 5. This ISQM <u>SQMS</u> applies to all firms performing audits or reviews of financial statements, or other assurance or related services engagements (i.e.,</p>	<p>Specific to U.S.</p>

² See, for example, International Standard on Auditing (ISA) 220 (Revised), *Quality Management for an Audit of Financial Statements* (Revised), paragraph 3

[‡] All AT-C sections can be found in *AICPA Professional Standards*.

[‡] All AR-C sections can be found in *AICPA Professional Standards*.

<p>if the firm performs any of these engagements, this ISQM applies <u>that perform any engagement included in a firm’s accounting and auditing practice.</u> The system of quality management that is established in accordance with the requirements of this ISQM<u>SQMS</u> enables the consistent performance by the firm of all such engagements).</p>	
<p>The Firm’s System of Quality Management</p>	
<p>7. 6-A system of quality management operates in a continual and iterative manner and is responsive to changes in the nature and circumstances of the firm and its engagements. It also does not operate in a linear manner. However, for the purposes of this ISQM<u>SQMS</u>, a system of quality management addresses the following eight components: (Ref: par. A3<u>2</u>)</p>	
<p>a. The firm’s risk assessment process;</p>	
<p>b. Governance and leadership;</p>	
<p>c. Relevant ethical requirements;</p>	
<p>d. Acceptance and continuance of client relationships and specific engagements;</p>	
<p>e. Engagement performance;</p>	
<p>f. Resources;</p>	
<p>g. Information and communication;</p>	
<p>h. The monitoring and remediation process-</p>	
<p>8. 7-This ISQM<u>SQMS</u> requires the firm to apply a risk-based approach in designing, implementing, and operating the components of the system of quality management in an interconnected and coordinated manner such that the firm proactively manages the quality of engagements performed by the firm. (Ref: par. A4<u>3</u>)</p>	
<p>9. 8-The risk-based approach is embedded in the requirements of this ISQM<u>SQMS</u> through <u>the following</u>:</p>	<p>AICPA style</p>
<p>a. <i>Establishing quality objectives.</i> The quality objectives established by the firm consist of objectives in relation to the components of the system of quality management that are to be achieved by the firm. The firm is required to establish the quality objectives specified by this ISQM<u>SQMS</u> and any additional quality objectives considered necessary by the firm to achieve the objectives of the system of quality management.</p>	

<p>b. <i>Identifying and assessing risks to the achievement of the quality objectives</i> (referred to in this standard <u>SQMS</u> as <i>quality risks</i>). The firm is required to identify and assess quality risks to provide a basis for the design and implementation of responses.</p>	
<p>c. <i>Designing and implementing responses to address the quality risks</i>. The nature, timing, and extent of the firm’s responses to address the quality risks are based on, and are responsive to, the reasons for the assessments given to the quality risks.</p>	
<p>10. 9. This ISQM <u>SQMS</u> requires that, at least annually, the individual(s) <u>or individuals</u> assigned ultimate responsibility and accountability for the system of quality management, on behalf of the firm, evaluates <u>evaluate</u> the system of quality management and concludes <u>conclude</u> whether the system of quality management provides the firm with reasonable assurance that the objectives of the system, stated in paragraph 44(a) and (15a-b), are being achieved. (Ref: par. A54)</p>	<p>AICPA style</p>
<p><i>Scalability</i></p>	
<p>11. 10. In applying a risk-based approach, the firm is required to take into account:</p>	
<p>a. the nature and circumstances of the firm; and</p>	
<p>b. the nature and circumstances of the engagements performed by the firm.</p>	
<p>Accordingly, the design of the firm’s system of quality management, ___ in particular, the complexity and formality of the system, ___ will vary. For example, a firm that performs different types of engagements for a wide variety of entities, including such as audits of financial statements of listed <u>specialized industries or group audits for multinational</u> entities, will likely need to have a more complex and formalized system of quality management and supporting documentation, 7 than a firm that performs only reviews of financial statements or compilation engagements.</p>	<p>Specific to ASB jurisdiction</p>
<p><i>Networks and Service Providers</i></p>	
<p>12. 11. This ISQM <u>SQMS</u> addresses the firm’s responsibilities when the firm:</p>	
<p>a. belongs to a network, and the firm complies with network requirements or uses network services in the system of quality management or in the performance of <u>performing</u> engagements; or</p>	<p>To clarify; no change in application</p>

<p><i>b.</i> uses resources from a service provider in the system of quality management or in the performance of<u>performing</u> engagements.</p>	intended
<p>Even when the firm complies with network requirements or uses network services or resources from a service provider, the firm is responsible for its system of quality management.</p>	
<p>Authority of This ISQM<u>Standard</u></p>	
<p>13. 42-Paragraph 44<u>15</u> contains the objective of the firm in following this ISQMS<u>SQMS</u>. This ISQMS<u>SQMS</u> contains <u>the following</u>: (Ref: par. <u>A5</u>)</p>	
<p><i>a.</i> Requirements designed to enable the firm to meet the objective in paragraph 44<u>15</u>; (Ref: par. A6<u>A7</u>A6)</p>	
<p><i>b.</i> Related guidance in the form of application and other explanatory material; (Ref: par. A8<u>A7</u>)</p>	
<p><i>c.</i> Introductory material that provides context relevant to a proper understanding of this ISQM; and<u>SQMS</u></p>	
<p><i>d.</i> Definitions- (Ref: par. A9<u>A8</u>)</p>	
<p>Effective Date</p>	
<p>14. 13-Systems of quality management in compliance with this ISQMS<u>SQMS</u> are required to be designed and implemented by December 15, 2022<u>2025</u>, and the evaluation of the system of quality management required by paragraphs 53-54 of this ISQM<u>55</u> is required to be performed within one year following December 15, 2022<u>2025</u>.</p>	
<p>Objective</p>	
<p>15. 14-The objective of the firm is to design, implement, and operate a system of quality management for audits or reviews of financial statements, or other assurance or related services engagements performed by the firm, <u>in its accounting and auditing practice</u> that provides the firm with reasonable assurance that:</p>	
<p><i>a.</i> the firm and its personnel fulfill their responsibilities in accordance with professional standards and applicable legal and regulatory requirements, and conduct engagements in accordance with such standards and requirements; and</p>	

<p>b. engagement reports issued by the firm or engagement partners are appropriate in the circumstances.</p>	<p>Reports in the U.S. are issued by firms, not engagement partners.</p>
<p>16. 15. The public interest is served by the consistent performance of quality engagements. The design, implementation, and operation of the system of quality management enables the consistent performance of quality engagements by providing the firm with reasonable assurance that the objectives of the system of quality management, stated in paragraph 14(a) and (15a-b), are achieved. Quality engagements are achieved through planning and performing engagements and reporting on them in accordance with professional standards and applicable legal and regulatory requirements. Achieving the objectives of those standards and complying with the requirements of applicable law or regulation involves exercising professional judgment and, when applicable to the type of engagement, exercising <u>maintaining</u> professional skepticism.</p>	<p>ASB preferred wording</p>
<p>Definitions</p>	
<p>17. 16. For purposes of this ISQM <u>the SQMSs</u>, the following terms have the meanings attributed below <u>as follows</u>:</p>	
<p><u>Accounting and auditing practice. A practice that performs engagements covered by this SQMS, which are audit, attestation, review, compilation, and any other services for which standards have been promulgated by the AICPA Auditing Standards Board (ASB) or the AICPA Accounting and Review Services Committee (ARSC) under the “General Standards Rule” (ET sec. 1.300.001)[†] or the “Compliance With Standards Rule” (ET sec. 1.310.001) of the AICPA code. (Ref: par. A9)</u></p>	<p>Specific to ASB jurisdiction</p>
<p>(a) Deficiency in the firm’s system of quality management (referred to as “deficiency” in this ISQM) <u>SQMS</u>— This exists when: (Ref: par. A10, and A159174–A160175)</p>	
<ul style="list-style-type: none"> • i. <u>i.</u> a quality objective required to achieve the objective of the system of quality management is not established; 	
<ul style="list-style-type: none"> • ii. <u>ii.</u> a quality risk, or combination of quality risks, is not identified or properly assessed; (Ref: par. A11) 	

[†] All ET sections can be found in [AICPA Professional Standards](#).

<ul style="list-style-type: none"> • iii. a response, or combination of responses, does not reduce to an acceptably low level the likelihood of a related quality risk occurring because the response(s) is <u>responses are</u> not properly designed, implemented, or operating effectively; or 	
<ul style="list-style-type: none"> • iv. An other <u>another</u> aspect of the system of quality management is absent, or not properly designed, implemented, or operating effectively, such that a requirement of this ISQM <u>SQMS</u> has not been addressed. (Ref: par. A12-<u>A13</u>) 	
<p>(b) Engagement documentation—<u>2</u> The record of work performed, results obtained, and conclusions the practitioner reached (terms such as “<i>working papers</i>” or “<i>work papers</i>” are sometimes used).</p>	
<p>(c) Engagement partner³—<u>2</u> The partner or other individual, appointed by the firm, who is responsible for the engagement and its performance, and for the report that is issued on behalf of the firm, and who, where <u>when</u> required, has the appropriate authority from a professional, legal, or regulatory body.</p>	AICPA style
<p>(d) Engagement quality review—<u>2</u> An objective evaluation of the significant judgments made by the engagement team and the conclusions reached thereon, performed by the engagement quality reviewer and completed on or before the date of the engagement report.</p>	
<p>(e) Engagement quality reviewer—<u>2</u> A partner, other individual in the firm, or an external individual, appointed by the firm to perform the engagement quality review.</p>	
<p>(f) Engagement team—<u>2</u> All partners and staff performing the engagement, and any other individuals who perform procedures on the engagement, excluding an external expert⁴ <u>specialist</u>¹ and internal auditors who provide direct assistance on an engagement. (Ref: par. A13<u>14</u>)</p>	ASB preferred word
<p>(g) External inspections—<u>2</u> Inspections or investigations, undertaken by an external oversight authority, related to the firm’s system of quality management or engagements performed by the firm. (Ref: par. A14<u>15</u>)</p>	

³ “Engagement partner” and “partner” is to be read as referring to their public sector equivalents where relevant.

⁴ ISA¹ Paragraph .06 of AU-C section 620, *Using the Work of an Auditor’s Expert*, paragraph 6(a) Specialist, defines the term “auditor’s ~~expert~~ specialist.”

<p>(h) Findings (in relation to a system of quality management)– Information about the design, implementation, and operation of the system of quality management that has been accumulated from the performance of monitoring activities, external inspections, and other relevant sources, which indicates that one or more deficiencies may exist. (Ref: par. A15<u>16</u>–A17–<u>18</u>)</p>	
<p>(i) Firm — A sole practitioner, partnership or corporation or other entity of professional accountants, or public sector equivalent. (Ref: par. A18) <u>Firm. A form of organization permitted by law or regulation whose characteristics conform to resolutions of the Council of the AICPA and that is engaged in public practice. (Ref: par. A19)</u></p>	<p>Specific to ASB jurisdiction</p>
<p><u>Inspection. Inspection is an evaluation of the adequacy of aspects of the firm’s quality management policies and procedures, its personnel’s understanding of those policies and procedures, and the extent of the firm’s compliance with them.</u></p>	<p>From extant QC section 10</p>
<p>(j) Listed entity — An entity whose shares, stock or debt are quoted or listed on a recognized stock exchange, or are marketed under the regulations of a recognized stock exchange or other equivalent body.</p>	<p>Specific to ASB jurisdiction</p>
<p>(l) Network — A larger structure: (Ref: par. A19) <u>Network. As defined in “Definitions” (ET sec. 0.400) in the AICPA code, an association of entities that includes one or more firms. (Ref: par. A20)</u></p>	<p>Specific to ASB jurisdiction</p>
<p>(k) Network firm — A firm or entity that belongs to the firm’s network. i. That is aimed at cooperation; and ii. That is clearly aimed at profit or cost-sharing or shares common ownership, control or management, common quality management policies or procedures, common business strategy, and use of a common brand name, or a significant part of professional resources <u>Network firm. As defined in “Definitions” (ET sec. 0.400) in the AICPA, a firm or other entity that belongs to a network. References to a network firm are to be read hereafter as “another firm or entity that belongs to the same network as the firm.”</u></p>	<p>Specific to ASB jurisdiction</p>
<p>(m) Partner– Any individual with authority to bind the firm with respect to the performance of a professional services engagement. <u>For purposes of this definition, partner may include an employee with this authority who has not</u></p>	<p>Specific to ASB jurisdiction</p>

<p><u>assumed the risks and benefits of ownership. Firms might use different titles to refer to individuals with this authority.</u></p>	
<p>(#) Personnel— Partners and staff in the firm. (Ref: par. A20–A21–<u>A22</u>)</p>	
<p>(e) Professional judgment— The application of relevant training, knowledge, and experience, within the context of professional standards, in making informed decisions about the courses of action that are appropriate in the design, implementation, and operation of the firm’s system of quality management.</p>	
<p>(p) Professional standards— IAASB Engagement Standards, as defined in the IAASB’s Preface to the International Quality Management, promulgated by the ASB or ARSC under the “General Standards Rule” (ET sec. 1.300.001) or the “Compliance With Standards Rule” (ET sec. 1.310.001) of the AICPA code or other standard-setting bodies that set auditing, Review, Other Assurance, and Related Services Pronouncements, and attest standards applicable to the <u>engagement being performed</u> and relevant ethical requirements.</p>	<p>Specific to ASB jurisdiction</p>
<p>(e) Quality objectives— The desired outcomes in relation to the components of the system of quality management to be achieved by the firm.</p>	
<p>(#) Quality risk— A risk that has a reasonable possibility of:</p>	
<ul style="list-style-type: none"> • i-occurring; and 	
<ul style="list-style-type: none"> • ii-individually, or in combination with other risks, adversely affecting the achievement of one or more quality objectives. 	
<p>(e) Reasonable assurance— In the context of the ISQMs<u>SQMSs</u>, a high, but not absolute, level of assurance.</p>	
<p>(t) Relevant ethical requirements— Principles of professional ethics and ethical requirements that are applicable to professional accountants<u>to which the firm, engagement team, engagement quality reviewer, and other firm personnel are subject</u> when undertaking engagements that are audits or reviews of financial statements or other assurance or related services engagements. Relevant ethical requirements ordinarily comprise the provisions<u>in the firm’s accounting and auditing practice that consist</u> of the IESBA<u>AICPA</u> code related to audits or reviews of financial statements, or other assurance or related services engagements, together with national requirements<u>together with rules of applicable state boards of accountancy and applicable regulatory agencies</u> that are more restrictive. (Ref: par. A223–A24, and A62<u>64</u>)</p>	<p>Specific to ASB jurisdiction</p>

<p>(u) Response (in relation to a system of quality management)— Policies or procedures designed and implemented by the firm to address one or more quality risk(s) <u>risks such as the following</u>: (Ref: par. A25–A27, and A5052)</p>	<p>AICPA style</p>
<ul style="list-style-type: none"> <u>i.</u> Policies are statements of what should, or should not, be done to address a quality risk(s) <u>risks</u>. Such statements may be documented, explicitly stated in communications, or implied through actions and decisions. 	<p>AICPA style</p>
<ul style="list-style-type: none"> <u>ii.</u> Procedures are actions to implement policies. 	
<p>(v) Service provider (in the context of this ISQM <u>SQMS</u>)— An individual or organization external to the firm that provides a resource that is used in the system of quality management or in the performance of <u>performing</u> engagements. Service providers exclude the firm’s network, other network firms, or other structures or organizations in the network. (Ref: par. A28, and A405110)</p>	<p>To clarify; no change in application intended</p>
<p>(w) Staff— Professionals, other than partners, including any experts <u>specialists</u> the firm employs.</p>	
<p>(x) System of quality management— A system designed, implemented, and operated by a firm to provide the firm with reasonable assurance that:</p>	
<ul style="list-style-type: none"> <u>a.</u> i. the firm and its personnel fulfill their responsibilities in accordance with professional standards and applicable legal and regulatory requirements, and conduct engagements in accordance with such standards and requirements; and 	
<ul style="list-style-type: none"> <u>b.</u> ii. engagement reports issued by the firm or engagement partners are appropriate in the circumstances. 	<p>See par. 15b</p>
<p>Requirements</p>	
<p>Applying, and Complying With, Relevant Requirements</p>	
<p>18. 47.—The firm shall <u>should</u> comply with each requirement of this ISQM <u>SQMS</u> unless the requirement is not relevant to the firm because of the nature and circumstances of the firm or its engagements. (Ref: par. A29)</p>	<p>ASB preferred wording</p>
<p>19. 48.—The individual (s) <u>or individuals</u> assigned ultimate responsibility and accountability for the firm’s system of quality management, and the individual (s) <u>or individuals</u> assigned operational responsibility for the firm’s system of quality management shall, <u>should</u> have an understanding</p>	<p>AICPA style</p>

<p>of this ISQM<u>SQMS</u>, including the application and other explanatory material, to understand the objective of this ISQM<u>SQMS</u> and to apply its requirements properly.</p>	
<p>System of Quality Management</p>	
<p>20. 19.The firm shall<u>should</u> design, implement, and operate a system of quality management. In doing so, the firm shall<u>should</u> exercise professional judgment, taking into account the nature and circumstances of the firm and its engagements. The governance and leadership component of the system of quality management establishes the environment that supports the design, implementation, and operation of the system of quality management. (Ref: par. A30–A31)</p>	
<p>Responsibilities</p>	
<p>21. 20.The firm shall<u>should</u> assign: (Ref: par. A32–A35<u>36</u>)</p>	
<p>a. ultimate responsibility and accountability for the system of quality management to the firm’s chief executive officer<u>CEO</u> or the firm’s managing partner (or equivalent) or, if appropriate, the firm’s managing board of partners (or equivalent);</p>	<p>AICPA style</p>
<p>b. operational responsibility for the system of quality management; <u>and</u></p>	
<p>c. operational responsibility for specific aspects of the system of quality management, including:</p>	
<p>i. compliance with independence requirements; <u>and</u> (Ref: par. A36<u>37</u>)</p>	
<p>ii. the monitoring and remediation process.</p>	
<p>22. 21.In assigning the roles in paragraph 20<u>21</u>, the firm shall<u>should</u> determine that the individual(s) <u>or individuals</u> (Ref: par. A37<u>par. A38</u>)</p>	
<p>a. Has<u>have</u> the appropriate experience, knowledge, influence, and authority within the firm, and sufficient time, to fulfill their assigned responsibility; <u>and</u> (Ref: par. A38<u>par. A39</u>)</p>	<p>AICPA style</p>
<p>b. Understands<u>understand</u> their assigned roles and that they are accountable for fulfilling them.</p>	<p>AICPA style</p>

<p>23. 22.–The firm shall<u>should</u> determine that the individual(s) <u>or individuals</u> assigned operational responsibility for the system of quality management, compliance with independence requirements, and the monitoring and remediation process, have a direct line of communication to the individual(s) <u>or individuals</u> assigned ultimate responsibility and accountability for the system of quality management.</p>	
<p>The Firm’s Risk Assessment Process</p>	
<p>24. 23.–The firm shall<u>should</u> design and implement a risk assessment process to establish quality objectives, identify and assess quality risks, and design and implement responses to address the quality risks. (Ref: par. A3940–A4442)</p>	
<p>25. 24.–The firm shall<u>should</u> establish the quality objectives specified by this ISQM<u>SQMS</u> and any additional quality objectives considered necessary by the firm to achieve the objectives of the system of quality management. (Ref: par. A4243–A4445)</p>	
<p>26. 25.–The firm shall<u>should</u> identify and assess quality risks to provide a basis for the design and implementation of responses. In doing so, the firm shall<u>should do the following</u>:</p>	<p>AICPA style</p>
<p>a. Obtain an understanding of the conditions, events, circumstances, actions, or inactions that may adversely affect the achievement of the quality objectives, including <u>the following</u>: (Ref: par. A4546– A4748)</p>	
<p>i. With respect to the nature and circumstances of the firm, those relating to:</p>	
<p>(1) a. the complexity and operating characteristics of the firm;</p>	
<p>(2) b. the strategic and operational decisions and actions, business processes, and business model of the firm;</p>	
<p>(3) c. the characteristics and management style of leadership;</p>	
<p>(4) d. the resources of the firm, including the resources provided by service providers;</p>	
<p>(5) e. law, regulation, professional standards, and the environment in which the firm operates; and</p>	
<p>(6) f. in the case of a firm that belongs to a network, the nature and extent of the network requirements and network services, if any</p>	

<p>ii. With respect to the nature and circumstances of the engagements performed by the firm, those relating to:</p>	
<p>(1) a. the types of engagements performed by the firm and the reports to be issued; and</p>	
<p>(2) b. the types of entities for which such engagements are undertaken</p>	
<p>b. Take into account how, and the degree to which, the conditions, events, circumstances, actions, or inactions in paragraph 25(26a) may adversely affect the achievement of the quality objectives. (Ref: par. A4849-A50)</p>	
<p>27. 26. The firm shall<u>should</u> design and implement responses to address the quality risks in a manner that is based on, and responsive to, the reasons for the assessments given to the quality risks. The firm’s responses shall<u>also should</u> include the responses specified in paragraph 3435. <u>However, the responses specified in paragraph 35 alone are not sufficient to achieve the objectives of the system of quality management.</u> (Ref: par. A49-A51-<u>A53</u>)</p>	<p>Moved from application material to emphasize essential guidance.</p>
<p>28. 27. The firm shall<u>should</u> establish policies or procedures that are designed to identify information <u>indicating</u> that indicates additional quality objectives, or additional or modified quality risks or responses, are needed due to changes in the nature and circumstances of the firm or its engagements. If such information is identified, the firm shall<u>should</u> consider the information and, when appropriate; (Ref: par. A5254-<u>A5355</u>)</p>	<p>To clarify; no change in application intended</p>
<p>a. establish additional quality objectives or modify additional quality objectives already<u>previously</u> established by the firm; (Ref: par. A5456)</p>	<p>AICPA style</p>
<p>b. identify and assess additional quality risks, modify the quality risks, or reassess the quality risks; or</p>	
<p>c. design and implement additional responses, or modify the responses.</p>	
<p>Governance and Leadership</p>	
<p>29. 28. The firm shall<u>should</u> establish the following quality objectives that address the firm’s governance and leadership, which establishes the environment that supports the system of quality management:</p>	
<p>a. The firm demonstrates a commitment to quality through a culture</p>	

that exists throughout the firm, which recognizes and reinforces <u>the following</u> : (Ref: par. A 55 57–A 56 58)	
i. The firm’s role in serving the public interest by consistently performing quality engagements;	
ii. The importance of professional ethics, values, and attitudes;	
iii. The responsibility of all personnel for quality relating to the performance of engagements or activities within the system of quality management, and their expected behavior; and	
iv. The importance of quality in the firm’s strategic decisions and actions, including the firm’s financial and operational priorities.	
b. Leadership is responsible and accountable for quality. (Ref: par. A 57 59)	
c. Leadership demonstrates a commitment to quality through their <u>its</u> actions and behaviors. (Ref: par. A 58 60)	
d. The organizational structure and assignment of roles, responsibilities, and authority is appropriate to enable the design, implementation, and operation of the firm’s system of quality management. (Ref: par. A32, A33, A35, <u>and</u> A 59 61)	
e. Resource needs, including financial resources, are planned for, and resources are obtained, allocated, or assigned in a manner that is consistent with the firm’s commitment to quality. (Ref: par. A 60 62–A 61 63)	
Relevant Ethical Requirements	
30. 29. —The firm shall <u>should</u> establish the following quality objectives that address the fulfillment of responsibilities in accordance with relevant ethical requirements, including those related to independence: (Ref: par. A 62 64–A 64 , A66 <u>and</u> A68)	
a. The firm and its personnel:	
i. understand the relevant ethical requirements to which the firm and the firm’s engagements are subject; <u>and</u> (Ref: par. A 22 , A 24 23)	
ii. fulfill their responsibilities in relation to the relevant ethical requirements to which the firm and the firm’s engagements are subject.	
b. Others, including the network, network firms, individuals in the network or network firms, or service providers, who are subject to the	

relevant ethical requirements to which the firm and the firm's engagements are subject:	
i. understand the relevant ethical requirements that apply to them; ⁷² and (Ref: par. A2223, A24, A6567)	
ii. fulfill their responsibilities in relation to the relevant ethical requirements that apply to them. (Ref: par. A68)	
Acceptance and Continuance of Client Relationships and Specific Engagements	
31. 30. The firm shall should establish the following quality objectives that address the acceptance and continuance of client relationships and specific engagements:	
a. Judgments by the firm about whether to accept or continue a client relationship or specific engagement are appropriate based on <u>the following</u> :	
i. Information obtained about the nature and circumstances of the engagement and the integrity and ethical values of the client (including management, and, when appropriate, those charged with governance) that is sufficient to support such judgments; and (Ref: par. A6769–A7174)	
ii. The firm's ability to perform the engagement in accordance with professional standards and applicable legal and regulatory requirements. (Ref: par. A7275–A76)	
b. The financial and operational priorities of the firm do not lead to inappropriate judgments about whether to accept or continue a client relationship or specific engagement. (Ref: par. A7377– A7478)	
Engagement Performance	
32. 31. The firm shall should establish the following quality objectives that address the performance of quality engagements:	
a. Engagement teams understand and fulfill their responsibilities in connection with the engagements, including, as applicable, the overall responsibility of engagement partners for managing and achieving quality on the engagement and being sufficiently and appropriately involved throughout the engagement. (Ref: par. A7579)	

<p>b. The nature, timing, and extent of direction and supervision of engagement teams and review of the work performed is appropriate based on the nature and circumstances of the engagements and the resources assigned or made available to the engagement teams, and; the work performed by less experienced engagement team members is directed, supervised, and reviewed by moresuitably experienced engagement team members. (Ref: par. A7680–A7781)</p>	
<p>c. Engagement teams exercise appropriate professional judgment and, when applicable to the type of engagement, <u>maintain</u> professional skepticism. (Ref: par. A7882)</p>	<p>ASB preferred word</p>
<p>d. Consultation on difficult or contentious matters is undertaken, and the conclusions agreed <u>to</u> are implemented. (Ref: par. A7983–A8485)</p>	
<p>e. Differences of opinion within the engagement team, or between the engagement team and the engagement quality reviewer or individuals performing activities within the firm’s system of quality management, are brought to the attention of the firm and resolved. (Ref: par. A8286)</p>	
<p>f. Engagement documentation is assembled on a timely basis after the date of the engagement report, and is appropriately maintained and retained to meet the needs of the firm and comply with law, regulation, relevant ethical requirements, orand professional standards. (Ref: par. A8387–A8589)</p>	
<p>Resources</p>	
<p>33. 32.The firm shall<u>should</u> establish the following quality objectives that address appropriately obtaining, developing, using, maintaining, allocating, and assigning resources in a timely manner to enable the design, implementation, and operation of the system of quality management: (Ref: par. A8690–A8791)</p>	
<p><i>Human Resources</i></p>	
<p>a. Personnel are hired, developed, and retained and have the competence and capabilities to: (Ref: par. A8892–A9094)</p>	
<p>i. consistently perform quality engagements, including having knowledge or experience relevant to the engagements the firm performs; or</p>	
<p>ii. perform activities or carry out responsibilities in relation to</p>	

<p>the operation of the firm’s system of quality management.</p>	
<p>b. Personnel demonstrate a commitment to quality through their actions and behaviors, develop and maintain the appropriate competence to perform their roles, and are held accountable or recognized through timely evaluations, compensation, promotion, and other incentives. (Ref: par. A9495–A9397)</p>	
<p>c. Individuals are obtained from external sources (i.e. that is, the network, another network firm, or a service provider) when the firm does not have sufficient or appropriate personnel to enable the operation of firm’s system of quality management or performance of engagements. (Ref: par. A9498)</p>	
<p>d. Engagement team members are assigned to each engagement, including an engagement partner, who have appropriate competence and capabilities, including being given sufficient time, to consistently perform quality engagements, <u>are assigned to each engagement</u>. (Ref: par. A8892–A8993, A9599–A97101)</p>	<p>To clarify; no change in application intended</p>
<p>e. Individuals are assigned to perform activities within the system of quality management who have appropriate competence and capabilities, including sufficient time, to perform such activities <u>are assigned to perform activities within the system of quality management</u>.</p>	<p>To clarify; no change in application intended</p>
<p><i>Technological Resources</i></p>	
<p>f. Appropriate technological resources are obtained or developed, implemented, maintained, and used, to enable the operation of the firm’s system of quality management and the performance of engagements. (Ref: par. A98102–A404,106 and A404109)</p>	
<p><i>Intellectual Resources</i></p>	
<p>g. Appropriate intellectual resources are obtained or developed, implemented, maintained, and used, to enable the operation of the firm’s system of quality management and the consistent performance of quality engagements, and such intellectual resources are consistent with professional standards and applicable legal and regulatory requirements, where applicable. (Ref: par. A402107–A404109)</p>	
<p><i>Service Providers</i></p>	
<p>h. Human, technological, or intellectual resources from service providers are appropriate for use in the firm’s system of quality management and in the performance of<u>performing</u> engagements, taking into account the quality objectives in paragraph 32 (d),(e),(f) and (33d–g). (Ref: par. A405110–A408115)</p>	<p>To clarify; no change in application intended</p>

Information and Communication	
<p>34. 33. The firm shall<u>should</u> establish the following quality objectives that address obtaining, generating, or using information regarding the system of quality management, and communicating information within the firm and to external parties on a timely basis to enable the design, implementation, and operation of the system of quality management: (Ref: par. A409<u>116</u>)</p>	
<p><i>a.</i> The information system identifies, captures, processes, and maintains relevant and reliable information that supports the system of quality management, whether from internal or external sources. (Ref: par. A110<u>117</u>–A111<u>119</u>)</p>	
<p><i>b.</i> The culture of the firm recognizes and reinforces the responsibility of personnel to exchange information with the firm and with one another. (Ref: par. A112<u>120</u>)</p>	
<p><i>c.</i> Relevant and reliable information is exchanged throughout the firm and with engagement teams, including <u>the following</u>: (Ref: par. A112<u>120</u>)</p>	
<p><i>i.</i> Information is communicated to personnel and engagement teams, and the nature, timing, and extent of the information is sufficient to enable them to understand and carry out their responsibilities relating to performing activities within the system of quality management or engagements; and.</p>	
<p><i>ii.</i> Personnel and engagement teams communicate information to the firm when performing activities within the system of quality management or engagements.</p>	
<p><i>d.</i> Relevant and reliable information is communicated to external parties, including <u>the following</u>:</p>	
<p><i>i.</i> Information is communicated by the firm to or within the firm’s network or to service providers, if any, enabling the network or service providers to fulfill their responsibilities relating to the network requirements or network services or resources provided by them; and. (Ref: par. A113<u>121</u>)</p>	
<p><i>ii.</i> Information is communicated externally when required by law, regulation, or professional standards, or to support external parties’ understanding of the system of quality management. (Ref: par. A114<u>122</u>–A115<u>123</u>)</p>	

Specified Responses	
<p>35. 34.—In designing and implementing responses in accordance with paragraph 26<u>27</u>, the firm shall<u>should</u> include the following responses: (Ref: par. A416<u>124</u>)</p>	
<p><i>a.</i> The firm establishes policies or procedures for:</p>	
<p style="padding-left: 40px;">i. identifying, evaluating, and addressing threats to compliance with the relevant ethical requirements; and. (Ref: par. A417<u>125</u>)</p>	
<p style="padding-left: 40px;">ii. identifying, communicating, evaluating, and reporting of any breaches of the relevant ethical requirements and appropriately responding to the causes and consequences of the breaches in a timely manner. (Ref: par. A418<u>126</u>–A419<u>127</u>)</p>	
<p><i>b.</i> The firm obtains, at least annually, a documented confirmation of compliance with independence requirements from all personnel required by relevant ethical requirements to be independent.</p>	
<p><i>c.</i> The firm establishes policies or procedures for receiving, investigating, and resolving complaints and allegations about failures to perform work in accordance with professional standards and applicable legal and regulatory requirements; or non-compliance with the firm’s policies or procedures established in accordance with this ISQMS<u>SQMS</u>. (Ref: par. A420<u>128</u>–A421<u>129</u>)</p>	
<p><i>d.</i> The firm establishes policies or procedures that address <u>the following</u> circumstances when:</p>	
<p style="padding-left: 40px;">i. The firm becomes aware of information subsequent to accepting or continuing a client relationship or specific engagement that would have caused it to decline the client relationship or specific engagement had that information been known prior to accepting or continuing the client relationship or specific engagement; or. (Ref: par. A422<u>130</u>–A423<u>131</u>)</p>	
<p style="padding-left: 40px;">ii. The firm is obligated by law or regulation to accept a client relationship or specific engagement. (Ref: par. A423<u>132</u>–<u>A133</u>)</p>	
<p><i>e.</i> The firm establishes policies or procedures that: (Ref: par. A424<u>134</u>–A426)</p>	

<p>i. Require communication with those charged with governance when performing an audit of financial statements of listed entities about how the system of quality management supports the consistent performance of quality audit engagements; (Ref: par. A127–A129 137)</p>	<p>Not applicable to ASB jurisdiction</p>
<p>i. address when it is otherwise appropriate to communicate with external parties about the firm’s system of quality management; and (Ref: par. A130138–A140)</p>	<p>Word deleted as a consequence of deleting previous paragraph</p>
<p>ii. address the information to be provided when communicating externally in accordance with paragraphs 34(e)(i) and 34(e)(ii) <u>about the firm’s system of quality management</u>, including the nature, timing, and extent and appropriate form of communication. (Ref: par. A134141–A132142)</p>	<p>To clarify; no change in application intended</p>
<p>f. The firm establishes policies or procedures that address engagement quality reviews in accordance with ISQMS<u>SQMS No. 2</u>; and require an engagement quality review for <u>the following</u>:</p>	
<p>i. Audits of financial statements of listed entities;</p>	<p>Not applicable to ASB jurisdiction</p>
<p>ii. i. Audits or other engagements for which an engagement quality review is required by law or regulation; and (Ref: par. A133143)</p>	
<p>iii. ii. Audits or other engagements for which the firm determines that an engagement quality review is an appropriate response to address one or more quality risk(s). <u>risks</u> (Ref: par. A134–A137144–A147)</p>	
<p>Monitoring and Remediation Process</p>	
<p>36. 35. The firm shall<u>should</u> establish a monitoring and remediation process to: (Ref: par. A138148)</p>	
<p>a. provide relevant, reliable, and timely information about the design, implementation, and operation of the system of quality management.</p>	
<p>b. take appropriate actions to respond to identified deficiencies such that deficiencies are remediated on a timely basis.</p>	
<p><i>Designing and Performing Monitoring Activities</i></p>	

<p>37. 36.–The firm shall<u>should</u> design and perform monitoring activities to provide a basis for the identification of deficiencies.</p>	
<p>38. 37.–In determining the nature, timing, and extent of the monitoring activities, the firm shall<u>should</u> take <u>the following</u> into account: (Ref: par. A439<u>149</u>–A442<u>152</u>)</p>	
<p><i>a.</i> The reasons for the assessments given to the quality risks;</p>	
<p><i>b.</i> The design of the responses;</p>	
<p><i>c.</i> The design of the firm’s risk assessment process and monitoring and remediation process; (Ref: par. A443<u>153</u>–A444<u>155</u>)</p>	
<p><i>d.</i> Changes in the system of quality management; (Ref: par. A445<u>156</u>)</p>	
<p><i>e.</i> The results of previous monitoring activities, whether previous monitoring activities continue to be relevant in evaluating the firm’s system of quality management and whether remedial actions to address previously identified deficiencies were effective; and (Ref: par. A446<u>157</u>– A447<u>158</u>)</p>	
<p><i>f.</i> Other relevant information, including complaints and allegations about failures to perform work in accordance with professional standards and applicable legal and regulatory requirements or non-compliance with the firm’s policies or procedures established in accordance with this ISQMS<u>SQMS</u>, information from external inspections, and information from service providers. (Ref: par. A448<u>159</u>–A450<u>161</u>)</p>	
<p>39. 38.–The firm shall<u>should</u> include the inspection of completed engagements in its monitoring activities and shall<u>should</u> determine which engagements and engagement partners to select. In doing so, the firm shall<u>should</u> (Ref: par. A441<u>150</u> and A454<u>162</u>–A454<u>166</u>)</p>	
<p><i>a.</i> take into account the matters in paragraph 37<u>38</u>;</p>	
<p><i>b.</i> consider the nature, timing, and extent of other monitoring activities undertaken by the firm and the engagements and engagement partners subject to such monitoring activities; (Ref: par. A167<u>167</u>–A168<u>168</u>) and</p>	
<p><i>c.</i> select at least one completed engagement for each engagement partner on a cyclical basis determined by the firm.</p>	
<p>40. 39.–The firm shall<u>should</u> establish policies or procedures that:</p>	

<p>a. require the individuals performing the monitoring activities to have the competence and capabilities, including sufficient time, to perform the monitoring activities effectively; and</p>	
<p>b. address the objectivity of the individuals performing the monitoring activities. Such policies or procedures shall prohibit, based on the premise that objectivity is enhanced when the engagement team members or the engagement quality reviewer of an engagement from<u>are not involved in</u> performing any inspection of monitoring activities related to that engagement. (Ref: par. A455<u>169</u>– A456<u>173</u>)</p>	<p>The ASB concluded that it was not necessary to change existing practice because in the United States, the peer review process provides a safeguard and provides evidence whether the monitoring procedures are effective.</p>
<p><i>Evaluating Findings and Identifying Deficiencies</i></p>	
<p>41. 40.—The firm shall<u>should</u> evaluate findings to determine whether deficiencies exist, including in the monitoring and remediation process. (Ref: par. A457<u>174</u>–A462<u>178</u>)</p>	
<p><i>Evaluating Identified Deficiencies</i></p>	
<p>42. 41.—The firm shall<u>should</u> evaluate the severity and pervasiveness of identified deficiencies by: (Ref: par. A464<u>173</u>, A463<u>175</u>–A464<u>176</u>)</p>	
<p>a. investigating the root cause(s)<u>causes</u> of the identified deficiencies. In determining the nature, timing, and extent of the procedures to investigate the root cause(s)<u>causes</u>, the firm shall<u>should</u> take into account the nature of the identified deficiencies and their possible severity. (Ref: par. A465<u>177</u>–A469<u>181</u>)</p>	<p>AICPA style</p>
<p>b. evaluating the effect of the identified deficiencies, individually and in aggregate, on the system of quality management.</p>	
<p><i>Responding to Identified Deficiencies</i></p>	
<p>43. 42.—The firm shall<u>should</u> design and implement remedial actions to address identified deficiencies that are responsive to the results of the root cause analysis. (Ref: par. A470<u>182</u>–A472<u>184</u>)</p>	

<p>44. 43. The individual(s) <u>or individuals</u> assigned operational responsibility for the monitoring and remediation process shall<u>should</u> evaluate whether the remedial actions:</p>	<p>AICPA style</p>
<p>a. are appropriately designed to address the identified deficiencies and their related root cause(s)<u>causes</u> and determine that they have been implemented;and.</p>	<p>AICPA style</p>
<p>b. implemented to address previously identified deficiencies are effective.</p>	
<p>45. 44. If the evaluation indicates that the remedial actions are not appropriately designed and implemented or are not effective, the individual(s) <u>or individuals</u> assigned operational responsibility for the monitoring and remediation process shall<u>should</u> take appropriate action to determine that the remedial actions are appropriately modified such that they are effective.</p>	<p>AICPA style</p>
<p><i>Findings About a Particular Engagement</i></p>	
<p>46. 45. The firm shall<u>should</u> respond to circumstances when<u>in which</u> findings indicate that there is an engagement(s) for which <u>required</u> procedures required were omitted during the performance of the engagement(s), or <u>that</u> the report issued may be inappropriate. The firm’s response shall<u>should</u> include <u>the following</u>: (Ref: par. A473<u>185</u>)</p>	<p>AICPA style</p>
<p>a. Taking appropriate action to comply with relevant professional standards and applicable legal and regulatory requirements;and</p>	
<p>b. When the report is considered to be inappropriate, considering the implications and taking appropriate action, including considering whether to obtain legal advice.</p>	
<p><i>Ongoing Communication Related to Monitoring and Remediation</i></p>	
<p>47. 46. The individual(s) <u>or individuals</u> assigned operational responsibility for the monitoring and remediation process shall<u>should</u> communicate <u>the following</u> on a timely basis to the individual(s) <u>or individuals</u> assigned ultimate responsibility and accountability for the system of quality management and the individual(s) <u>or individuals</u> assigned operational responsibility for the system of quality management: (Ref: par. A474<u>186</u>)</p>	<p>AICPA style</p>
<p>a. A description of the monitoring activities performed;</p>	
<p>b. The identified deficiencies, including the severity and pervasiveness of such deficiencies;and</p>	

<p>c. The remedial actions to address the identified deficiencies-</p>	
<p>48. 47. The firm shall<u>should</u> communicate the matters described in paragraph 46<u>47</u> to engagement teams and other individuals assigned activities within the system of quality management to enable them to take prompt and appropriate action in accordance with their responsibilities.</p>	
<p>Network Requirements or Network Services</p>	
<p>49. 48. When the firm belongs to a network, the firm shall<u>should</u> understand <u>the following</u>, when applicable: (Ref: par. A19<u>20</u> and A175<u>187–A189</u>)</p>	
<p>a. The requirements established by the network regarding the firm’s system of quality management, including requirements for the firm to implement or use resources or services designed or otherwise provided by or through the network (i.e.that is, network requirements);</p>	
<p>b. Any services or resources provided by the network that the firm chooses to implement or use in the design, implementation, or operation of the firm’s system of quality management (i.e.that is, network services);and</p>	
<p>c. The firm’s responsibilities for any actions that are necessary to implement the network requirements or use network services. (Ref: par. A176<u>190</u>)</p>	
<p>The firm remains responsible for its system of quality management, including professional judgments made in the design, implementation, and operation of the system of quality management. The firm shall<u>should</u> not allow compliance with the network requirements or use of network services to contravene the requirements of this ISQMS<u>SQMS</u>. (Ref: par. A177<u>20</u> and A191)</p>	
<p>50. 49. Based on the understanding obtained in <u>accordance with</u> paragraph 48<u>49</u>, the firm shall:<u>should</u></p>	<p>To clarify</p>
<p>a. determine how the network requirements or network services are relevant to, and are taken into account in, the firm’s system of quality management, including how they are to be implemented;and. (Ref: par. A178<u>192</u>)</p>	
<p>b. evaluate whether and, if so, how the network requirements or network services need to be adapted or supplemented by the firm to be appropriate for use in its system of quality management. (Ref: par. A179<u>193–A180</u><u>195</u>)</p>	

<i>Monitoring Activities Undertaken by the Network on the Firm’s System of Quality Management</i>	
51. 50. In For circumstances when <u>in which</u> the network performs monitoring activities relating to the firm’s system of quality management, the firm shall: <u>should</u>	AICPA style
a. determine the effect of the monitoring activities performed by the network on the nature, timing, and extent of the firm’s monitoring activities performed in accordance with paragraphs 3637–3839 ;	
b. determine the firm’s responsibilities in relation to the monitoring activities, including any related actions by the firm; and	
c. as part of evaluating findings and identifying deficiencies in paragraph 4041 , obtain the results of the monitoring activities from the network in a timely manner. (Ref: par. A 184196)	
<i>Monitoring Activities Undertaken by the Network Across the Network Firms</i>	
52. 51. The firm shall: <u>should</u>	
a. understand the overall scope of the monitoring activities undertaken by the network across the network firms, including monitoring activities to determine that network requirements have been appropriately implemented across the network firms, and how the network will communicate the results of its monitoring activities to the firm ; ;	
b. at least annually, obtain information from the network about the overall results of the network’s monitoring activities across the network firms, if applicable, and: (Ref: par. A 182197–A184199)	
i. communicate the information to engagement teams and other individuals assigned activities within the system of quality management, as appropriate, to enable them to take prompt and appropriate action in accordance with their responsibilities ; ; and	
ii. consider the effect of the information on the firm’s system of quality management.	
<i>Deficiencies in Network Requirements or Network Services Identified by the Firm</i>	
53. 52. If the firm identifies a deficiency in the network requirements or network services, the firm shall: <u>should</u> (Ref: par. A 185200)	

<p>a. communicate to the network relevant information about the identified deficiency; and</p>	
<p>b. in accordance with paragraph 4243, design and implement remedial actions to address the effect of the identified deficiency in the network requirements or network services. (Ref: par. A486201)</p>	
<p>Evaluating the System of Quality Management</p>	
<p>54. 53. The individual(s) <u>or individuals</u> assigned ultimate responsibility and accountability for the system of quality management shall<u>should</u> evaluate, on behalf of the firm, the system of quality management. The evaluation shall<u>should</u> be undertaken as of a point in time; and performed at least annually. (Ref: par. A487<u>202</u>–A489<u>205</u>)</p>	
<p>55. 54. Based on the evaluation, the individual(s) <u>or individuals</u> assigned ultimate responsibility and accountability for the system of quality management shall<u>should</u> conclude, on behalf of the firm, one of the following: (Ref: par. A490<u>,206</u> and A495<u>213</u>)</p>	
<p>a. The system of quality management provides the firm with reasonable assurance that the objectives of the system of quality management are being achieved; (Ref: par. A491<u>207</u>)</p>	
<p>b. Except for matters related to identified deficiencies that have a severe but not pervasive effect on the design, implementation, and operation of the system of quality management, the system of quality management provides the firm with reasonable assurance that the objectives of the system of quality management are being achieved; or. (Ref: par. A492<u>208</u>)</p>	
<p>c. The system of quality management does not provide the firm with reasonable assurance that the objectives of the system of quality management are being achieved. (Ref: par. A492<u>208</u>– A494<u>212</u>)</p>	
<p>56. 55. If the individual(s) <u>or individuals</u> assigned ultimate responsibility and accountability for the system of quality management reaches the conclusion described in paragraph 54<u>(55b)</u> or 54<u>(55c)</u>, the firm shall<u>should do the following</u>: (Ref: par. A496<u>214</u>)</p>	
<p>a. Take prompt and appropriate action; and</p>	
<p>b. Communicate to:</p>	
<p>i. engagement teams and other individuals assigned activities</p>	

<p>within the system of quality management to the extent that it is relevant to their responsibilities; and (Ref: par. A197<u>215</u>)</p>	
<p>ii. external parties in accordance with the firm’s policies or procedures required by paragraph 34<u>(35e)</u>. (Ref: par. A198<u>216</u>)</p>	
<p>57. 56.–The firm shall<u>should</u> undertake periodic performance evaluations of the individual(s) <u>or individuals</u> assigned ultimate responsibility and accountability for the system of quality management; and the individual(s) <u>or individuals</u> assigned operational responsibility for the system of quality management. In doing so, the firm shall<u>should</u> take into account the evaluation of the system of quality management. (Ref: par. A199<u>217</u>–A204<u>219</u>)</p>	
<p>Documentation</p>	
<p>58. 57.–The firm shall<u>should</u> prepare documentation of its system of quality management that is sufficient to: (Ref: par. A202<u>220</u>–A204<u>222</u>)</p>	
<p>a. support a consistent understanding of the system of quality management by personnel, including an understanding of their roles and responsibilities with respect to the system of quality management and the performance of performing engagements; –;</p>	
<p>b. support the consistent implementation and operation of the responses; and .</p>	
<p>c. provide evidence of the design, implementation, and operation of the responses; to support the evaluation of the system of quality management by the individual(s) <u>or individuals</u> assigned ultimate responsibility and accountability for the system of quality management.</p>	
<p>59. 58.–In preparing documentation, the firm shall<u>should</u> include: –a. the <u>following</u>:</p>	
<p>a. Identification of the individual(s) <u>or individuals</u> assigned ultimate responsibility and accountability for the system of quality management and operational responsibility for the system of quality management;</p>	
<p>b. The firm’s quality objectives and quality risks; (Ref: par. A205<u>223</u>)</p>	
<p>c. A description of the responses and how the firm’s responses address the quality risks;</p>	

d. Regarding the monitoring and remediation process: ; _;	
i. evidence of the monitoring activities performed;	
ii. the evaluation of findings, and identified deficiencies and their related root cause(s) causes; <u>and</u>	
iii. remedial actions to address identified deficiencies and the evaluation of the design and implementation of such remedial actions; and.	
iv. Communications about monitoring and remediation; and	
e. The basis for conclusion reached pursuant to paragraph 54. <u>55</u> <u>and the basis for that conclusion</u>	To clarify; no change in application intended
60. 59. The firm shall <u>should</u> document the matters in paragraph 58 <u>59</u> as they relate to network requirements or network services and the evaluation of the network requirements or network services in accordance with paragraph 49 <u>(50b)</u> . (Ref: par. A 206 <u>224</u>)	
61. 60. The firm shall <u>should</u> establish a period of time for the retention of documentation for the system of quality management that is sufficient to enable the firm <u>and its peer reviewer</u> to monitor the design, implementation _, and operation of the firm’s system of quality management _, or for a longer period if required by law or regulation.	Specific to ASB jurisdiction
Application and Other Explanatory Material	
Scope of This ISQM<u>Standard</u> (Ref: par. 3–4)	
A1. Other pronouncements of the IAASB, including ISRE 2400 (Revised)⁵ and ISAE 3000 (Revised),⁶ also establish requirements for the engagement partner for the management of quality at the engagement level.	Not applicable in U.S.

⁵ ~~International Standard on Review Engagements (ISRE) 2400 (Revised), Engagements to Review Historical Financial Statements~~

⁶ ~~International Standard on Assurance Engagements (ISAE) 3000 (Revised), Assurance Engagements Other than Audits or Reviews of Historical Financial Information~~

<p>A1. A2. The IESBA AICPA code⁷ contains requirements and application material for professional accountants that enable professional accountants to meet their responsibility <u>establishes the fundamental principles of professional ethics, which include the obligation</u> to act in <u>a way that serves</u> the public interest.² As indicated in paragraph 45<u>16</u>, in the context of engagement performance as described in this ISQMS<u>SQMS</u>, the consistent performance of quality engagements forms part of the professional accountant's responsibility<u>obligation</u> to act in the public interest.</p>	<p>Specific to ASB jurisdiction</p>
<p>The Firm's System of Quality Management (Ref: par. 67-9<u>10</u>)</p>	
<p>A2. A3. The firm may use different terminology or frameworks to describe the components of its system of quality management.</p>	
<p>A3. A4. Examples of the interconnected nature of the components include the following:</p>	
<ul style="list-style-type: none"> • The firm's risk assessment process sets out the process the firm is required to follow in implementing a risk-based approach across the system of quality management. 	
<ul style="list-style-type: none"> • The governance and leadership component establishes the environment that supports the system of quality management. 	
<ul style="list-style-type: none"> • The resources and information and communication components enable the design, implementation, and operation of the system of quality management. 	
<ul style="list-style-type: none"> • The monitoring and remediation process is a process designed to monitor the entire system of quality management. The results of the monitoring and remediation process provide information that is relevant to the firm's risk assessment process. 	<p>To clarify</p>
<ul style="list-style-type: none"> • There may be relationships between specific matters⁷; for example, certain aspects of relevant ethical requirements are relevant to accepting and continuing client relationships and specific engagements. 	
<p>A4. A5. Reasonable assurance is obtained when the system of quality management reduces to an acceptably low level the risk that the objectives</p>	<p>To clarify</p>

⁷ ~~The International Ethics Standards Board for Accountants' International Code of Ethics for Professional Accountants (including International Independence Standards) (IESBA Code)~~

² Paragraph .01 of ET section 0.300.030.

<p>stated in paragraph 44(a) and (15a-b) are not achieved. Reasonable assurance is not an absolute level of assurance, because there are inherent limitations of a system of quality management. Such limitations include <u>the fact</u> that human judgment in decision making can be faulty and that breakdowns in a firm’s system of quality management may occur, for example, due to human error or behavior or failures in information technology (IT) applications.</p>	
<p>Authority of This ISQM<u>SQMS</u> (Ref: par. 42<u>13</u>)</p>	
<p>A5. A6.The objective of this ISQM<u>SQMS</u> provides the context in which the requirements of this ISQM<u>SQMS</u> are set, establishes the desired outcome of this ISQM<u>SQMS</u>, and is intended to assist the firm in understanding what needs to be accomplished and, where<u>when</u> necessary, the appropriate means of doing so.</p>	
<p>A6. A7.The requirements of this ISQM<u>SQMS</u> are expressed using “shall<u>the word should.</u>”</p>	<p>ASB preferred word</p>
<p>A7. A8.—Where<u>When</u> necessary, the application and other explanatory material provides further explanation of the requirements and guidance for carrying them out. In particular, it may:</p>	<p>AICPA style word</p>
<ul style="list-style-type: none"> • explain more precisely what a requirement means or is intended to cover; and 	
<ul style="list-style-type: none"> • include examples that illustrate how the requirements might be applied. 	
<p>While<u>Although</u> such guidance does not, in itself, impose a requirement, it is relevant to the proper application of the requirements. The application and other explanatory material may also provide background information on matters addressed in this ISQM. Where appropriate, additional considerations specific to public sector audit organizations are included within the application and other explanatory material<u>SQMS</u>. These additional considerations assist in the application of the requirements in this ISQM<u>SQMS</u>. They do not, however, limit or reduce the responsibility of the firm to apply and comply with the requirements in this ISQM<u>SQMS</u>.</p>	<p>Specific to ASB jurisdiction</p>
<p>A8. A9.This ISQM<u>SQMS</u> includes, under the heading “Definitions,” a description of the meanings attributed to certain terms for purposes of this ISQM<u>SQMS</u>. These definitions are provided to assist in the consistent application and interpretation of this ISQM<u>SQMS</u> and are not intended to override definitions that may be established for other purposes, whether in law, regulation, or otherwise. The Glossary of Terms relating to International Standards issued by the IAASB in the Handbook of International Quality Management, Auditing, Review, Other Assurance, and Related Services Pronouncements published by IFAC includes the terms defined in this ISQM. The Glossary of Terms also includes descriptions of other terms found in the ISQMs to assist in common and consistent interpretation and translation.</p>	<p>Specific to ASB jurisdiction</p>

Definitions	
<u>Accounting and Auditing Practice (Ref: par. 17)</u>	
<p>A9. <u>Standards promulgated by the ASB and ARSC that apply to engagements covered by this SQMS comprise the following:</u></p> <ul style="list-style-type: none"> • <u>Statements on Auditing Standards (SASs)</u> • <u>Statements on Standards for Attestation Engagements (SSAEs)</u> • <u>Statements on Standards for Accounting and Review Services (SSARSs)</u> <p><u>Although standards for other engagements may be promulgated by other AICPA technical committees, engagements performed in accordance with those standards are not encompassed in the definition of an <i>accounting and auditing practice</i>.</u></p>	Added to clarify
Deficiency (Ref: par. 16(a) <u>17</u>)	
A10. The firm identifies deficiencies through <u>by</u> evaluating findings. A deficiency may arise from a finding ; or a combination of findings.	
A11. When a deficiency is identified as a result of a quality risk, or combination of quality risks, not being identified or properly assessed, the response(s) <u>responses</u> to address such quality risk(s) <u>risks</u> may also be absent ; or not appropriately designed or implemented.	
A12. The other aspects of the system of quality management consist of the requirements in this ISQM <u>SQMS</u> addressing <u>the following</u> :	
<ul style="list-style-type: none"> • Assigning responsibilities (paragraphs 20<u>21</u>–22); • The firm’s risk assessment process; • The monitoring and remediation process;<u>and</u> • The evaluation of the system of quality management. 	
A13. Examples of deficiencies related to other aspects of the system of quality management <u>include the following</u> :	

<ul style="list-style-type: none"> • The firm’s risk assessment process fails to identify information that indicates changes in the nature and circumstances of the firm and its engagements and the need to establish additional quality objectives, or modify the quality risks or responses. 	
<ul style="list-style-type: none"> • The firm’s monitoring and remediation process is not designed or implemented in a manner that: <ul style="list-style-type: none"> ○ provides relevant, reliable, and timely information about the design, implementation, and operation of the system of quality management. ○ enables the firm to take appropriate actions to respond to identified deficiencies such that deficiencies are remediated on a timely basis. 	
<ul style="list-style-type: none"> • The individual(s) <u>or individuals</u> assigned ultimate responsibility and accountability for the system of quality management does<u>do</u> not undertake the annual evaluation of the system of quality management. 	
Engagement Team (Ref: par. 16(f)<u>17</u>)	
<p>A14. A13<u>SAS No. ISA 220 (Revised)</u>⁸<u>146</u>³ provides guidance in applying the definition of <i>engagement team</i> in the context of an audit of financial statements. <u>AU-C section 600, <i>Special Considerations — Audits of Group Financial Statements (Including the Work of Component Auditors)</i></u>,¹ <u>expands on how SAS No. 146 is to be applied in relation to an audit of group financial statements. The quality risks and responses to those risks relevant to group audit engagements may be different for engagement team members who are firm personnel than for engagement team members who are external to the firm (for example, engagement team members who are from network firms or are service providers, such as component auditors from firms not within the firm’s network).</u></p>	Added to clarify
External Inspections (Ref: par. 16(g)<u>17</u>)	
<p>A15. A14In some circumstances, an external oversight authority, <u>such as the U.S. Department of Labor</u>, may undertake other types of inspections, for</p>	

⁸ [ISA 220 \(Revised\), paragraphs A15–A25](#)³ [Paragraphs A15–A21 of Statement on Auditing Standards \(SAS\) No. 146, *Quality Management for an Engagement Conducted in Accordance With Generally Accepted Auditing Standards*.](#)

¹ [All AU-C sections can be found in AICPA Professional Standards.](#)

<p>example, thematic reviews that focus on, for a selection of firms, particular aspects of audit engagements or firm-wide practices.</p>	
<p>Findings (Ref: par. 16(h) <u>17</u>)</p>	
<p>A16. A15 As part of accumulating findings from monitoring activities, external inspections, and other relevant sources, the firm may identify other observations about the firm’s system of quality management, such as positive outcomes or opportunities for the firm to improve, or further enhance, the system of quality management. Paragraph A458<u>168</u> explains how other observations may be used by the firm in the system of quality management.</p>	
<p>A17. A16 Paragraph A448<u>157</u> provides examples of information from other relevant sources.</p>	
<p>A18. A17. Monitoring activities include monitoring at the engagement level, such as inspection of engagements. Furthermore, external inspections and other relevant sources may include information that relates to specific engagements. As a result, information about the design, implementation, and operation of the system of quality management includes engagement-level findings that may be indicative of findings in relation to the system of quality management.</p>	
<p>Firm (Ref: par. 16(i) <u>17</u>)</p>	
<p>A19. A18 The definition of “firm” in relevant ethical requirements may differ from the definition set out in this ISQMS<u>SQMS</u>.</p>	
<p>Network (Ref: par. 16(i), 48 <u>17 and 49</u>)</p>	
<p>A20. A19 Networks and the firms within the network may be structured in a variety of ways. For example, in the context of a firm’s system of quality management:–</p>	
<ul style="list-style-type: none"> the network may establish requirements for the firm related to its system of quality management; or provide services that are used by the firm in its system of quality management or in the performance of performing engagements;– 	
<ul style="list-style-type: none"> other firms within the network may provide services (e.g. for example, resources) that are used by the firm in its system of quality management or in the performance of performing engagements; or– 	

<ul style="list-style-type: none"> other structures or organizations within the network may establish requirements for the firm related to its system of quality management, or provide services. 	
<p>For the purposes of this ISQM <u>standard</u>, any network requirements or network services that are obtained from the network, another firm within the network, or another structure or organization in the network are considered “network requirements or network services.”</p>	
<p>Personnel (Ref: par. 16(n) <u>17</u>)</p>	
<p>A21. In addition to personnel (i.e. that is, individuals in the firm), the firm may use individuals external to the firm in performing activities in the system of quality management or in the performance of <u>performing</u> engagements. For example, individuals external to the firm may include individuals from other network firms (e.g. for example, individuals in a service delivery center of a network firm) or individuals employed by a service provider (e.g. for example, a component auditor from another firm not within the firm’s network).</p>	
<p>A22. A21. Personnel also includes partners and staff in other structures of the firm, such as a service delivery center in the firm.</p>	
<p>Relevant Ethical Requirements (Ref: par. 16(t), 29 <u>17 and 30</u>)</p>	
<p>A23. A22. The relevant ethical requirements that are applicable in the context of a system of quality management may vary, depending on the nature and circumstances of the firm and its engagements. The term “professional accountant” may be defined in relevant ethical requirements. For example, the IESBA Code defines the term “professional accountant” and further explains the scope of provisions in the IESBA Code that apply to individual professional accountants in public practice and their firms.</p>	<p>Specific to ASB jurisdiction</p>
<p>A23. The IESBA Code addresses circumstances when law or regulation precludes the professional accountant from complying with certain parts of the IESBA Code. It further acknowledges that some jurisdictions might have provisions in law or regulation that differ from or go beyond those set out in <u>AICPA code acknowledges that federal, state, or local statutes, rules, or regulations may be more restrictive than</u> the IESBA <u>AICPA</u> code and that professional accountants in those jurisdictions need to be aware of these differences and comply with the more stringent provisions, unless prohibited by law or regulation.</p>	<p>Specific to ASB jurisdiction</p>
<p>A24. Various provisions of the relevant ethical requirements may apply only to individuals in the context of the performance of engagements and not the firm itself. For example:</p>	

<p>• Part 2 of the IESBA Code applies to individuals who are professional accountants in public practice when they are performing professional activities pursuant to their relationship with the firm, whether as a contractor, employee or owner, and may be relevant in the context of the performance of engagements.</p>	<p>Specific to ASB jurisdiction</p>
<p>• Certain requirements in Parts 3 and 4 of the IESBA Code also apply to individuals who are professional accountants in public practice when they are performing professional activities for clients., <u>the “Integrity and Objectivity Rule” of the AICPA code (ET sec. 1.100.001) prohibits individuals from knowingly misrepresenting facts or subordinating their judgment when performing professional services for a client or for an employer.</u> Compliance with such relevant ethical requirements by individuals may need to be addressed by the firm’s system of quality management.</p>	<p>Specific to ASB jurisdiction</p>
<p>Example of relevant ethical requirements that are applicable only to individuals and not the firm, and which relate to the performance of engagements</p> <p>Part 2 of the IESBA Code addresses pressure to breach the fundamental principles, and includes requirements that an individual shall not:</p> <ul style="list-style-type: none"> • Allow pressure from others to result in a breach of compliance with the fundamental principles; or • Place pressure on others that the accountant knows, or has reason to believe, would result in the other individuals breaching the fundamental principles. <p>For example, circumstances may arise when, in performing an engagement, an individual considers that the engagement partner or another senior member of the engagement team has pressured them to breach the fundamental principles.</p>	<p>Specific to ASB jurisdiction</p>
<p>Response (Ref: par. 16(u). <u>17</u>)</p>	
<p>A25. Policies are implemented through the actions of personnel and other individuals whose actions are subject to the policies (including engagement teams), or through their restraint from taking actions that would conflict with the firm’s policies.</p>	
<p>A26. Procedures may be mandated, through formal documentation or other communications, or may result from behaviors that are not mandated but are, rather, <u>are</u> conditioned by the firm’s culture. Procedures may be enforced through the actions permitted by IT applications, or other aspects of the firm’s IT environment.</p>	
<p>A27. If the firm uses individuals external to the firm in the system of quality management or in the performance of <u>performing</u> engagements, different policies</p>	

<p>or procedures may need to be designed by the firm to address the actions of the individuals. ISA 220 (Revised)⁹ SAS No. 146⁵ provides guidance when different policies or procedures may need to be designed by the firm to address the actions of individuals external to the firm in the context of an audit of financial statements.</p>	
<p>Service Provider (Ref: par. 16(v) 17)</p>	
<p>A28. Service providers include component auditors from other firms not within the firm’s network.</p>	
<p>Applying, and Complying With, Relevant Requirements (Ref: par. 17 18)</p>	
<p>A29. Examples of when a requirement of this ISQMSQMS may not be relevant to the firm include the following:</p>	
<ul style="list-style-type: none"> • The firm is a sole practitioner. For example, the requirements addressing the organizational structure and assigning roles, responsibilities, and authority within the firm; direction, supervision, and review; and addressing differences of opinion may not be relevant. 	
<ul style="list-style-type: none"> • The firm only performs engagements that are related servicespreparation of financial statements engagements in accordance with AR-C section 70, Preparation of Financial Statements. For example, because the firm is not required to maintain independence for related servicespreparation of financial statements engagements, the requirement to obtain a documented confirmation of compliance with independence requirements from all personnel would not be relevant. 	<p>Specific to ASB jurisdiction</p>
<p>System of Quality Management</p>	
<p>Design, Implement, and Operate a System of Quality Management (Ref: par. 19 20)</p>	
<p>A30. Quality management is not a separate function of the firm; it is the integration of a culture that demonstrates a commitment to quality with the firm’s strategy, operational activities, and business processes. As a result, designing the system of quality management and the firm’s operational activities and business processes in an integrated manner may promote a</p>	

⁹ ~~ISA 220 (Revised)~~,⁵ Paragraphs A23–A25 [of SAS No. 146](#).

<p>harmonious approach to managing the firm, and enhance the effectiveness of quality management.</p>	
<p>A31. The quality of professional judgments exercised by the firm is likely to be enhanced when individuals making such judgments demonstrate an attitude that includes an inquiring mind, which involves:</p>	
<ul style="list-style-type: none"> • considering the source, relevance, and sufficiency of information obtained about the system of quality management, including information related to the nature and circumstances of the firm and its engagements; and 	
<ul style="list-style-type: none"> • being open and alert to a need for further investigation or other action. 	
<p>Responsibilities (Ref: par. 20-21, 28(-22 and 29d))</p>	
<p>A32. The governance and leadership component includes a quality objective that the firm has an organizational structure and assignment of roles, responsibilities, and authority that is appropriate to enable the design, implementation, and operation of the firm’s system of quality management.</p>	
<p>A33. Notwithstanding the assignment of responsibilities related to the system of quality management in accordance with paragraph 2021, the firm remains ultimately responsible for the system of quality management and holding individuals responsible and accountable for their assigned roles. For example, in accordance with paragraphs 5354 and 5455, although the firm assigns the evaluation of the system of quality management and conclusion thereon to the individual(s) or individuals assigned ultimate responsibility and accountability for the system of quality management, the firm is responsible for the evaluation and conclusion.</p>	
<p>A34. An individual(s) assigned responsibility for the matters in paragraph 20 is typically a partner of the firm so that they Individuals who have the appropriate influence and authority within the firm, as required by paragraph 2422, to be assigned responsibility for the matters in paragraph 21 are typically partners of the firm. However, based on the legal structure of the firm, there may be circumstances when in which an individual(s) may not be a partner of the firm, but the individual(s) has the appropriate influence and authority within the firm to perform their the assigned role because of formal arrangements made by the firm or the firm’s network.</p>	
<p>A35. How the firm assigns roles, responsibilities, and authority within the firm may vary, and law or regulation may impose certain requirements for the firm that affect the leadership and management structure or their assigned</p>	

<p>responsibilities. An individual(s) assigned responsibility for a matter(s) in paragraph 20<u>21</u> may further assign roles, procedures, tasks, or actions to other individuals to assist them<u>the individual</u> in fulfilling their<u>the</u> responsibilities. However, an individual(s) assigned responsibility for a matter(s) in paragraph 20<u>22</u> remains responsible and accountable for the responsibilities assigned to them<u>the individual</u>.</p>	
<p>A36. <u>An example of</u> scalability example to demonstrate how assigning roles and responsibilities may be undertaken <u>in firms of different complexity is as follows:</u></p>	
<ul style="list-style-type: none"> • In a less complex firm, ultimate responsibility and accountability for the system of quality management may be assigned to a single managing partner with sole responsibility for the oversight of the firm. This individual may also assume responsibility for all aspects of the system of quality management, including operational responsibility for the system of quality management, compliance with independence requirements, and the monitoring and remediation process. 	
<ul style="list-style-type: none"> • In a more complex firm, there may be multiple levels of leadership that reflect the organizational structure of the firm <u>may include the multiple levels of leadership</u>, and the firm may have an independent governing body that has non-executive oversight of the firm, which may comprise external individuals. Furthermore, the firm may assign operational responsibility for specific aspects of the system of quality management beyond those specified in paragraph 20<u>(21c)</u>, such as operational responsibility for compliance with ethical requirements or operational responsibility for managing a service line. 	<p>To clarify; no change in application intended</p>
<p>A37. A36.—Compliance with independence requirements is essential to the performance of audits, or reviews of financial statements, or other assurance engagements, <u>in a firm’s accounting and auditing practice</u> and is an expectation of stakeholders relying on the firm’s reports. The individual(s) <u>or individuals</u> assigned operational responsibility for compliance with independence requirements is<u>are</u> ordinarily responsible for the oversight of all matters related to independence so that a robust and consistent approach is designed and implemented by the firm to deal with independence requirements.</p>	
<p>A38. A37.—Law, regulation, or professional standards may establish additional requirements for an individual assigned responsibility for a matter(s) in paragraph 20<u>21</u>, such as requirements for professional licensing, professional education, or continuing professional development.</p>	

<p>A39. A38.—The appropriate experience and knowledge for the individual(s) <u>or individuals</u> assigned operational responsibility for the system of quality management ordinarily includes an understanding of the firm’s strategic decisions and actions and experience with the firm’s business operations.</p>	
<p>The Firm’s Risk Assessment Process (Ref: par. <u>2324</u>)</p>	
<p>A40. A39.—How the firm designs the firm’s risk assessment process may be affected by the nature and circumstances of the firm, including how the firm is structured and organized. <u>Examples of scalability</u> examples to demonstrate how the firm’s risk assessment process may differ <u>from that of other firms include the following:</u></p>	<p>To clarify</p>
<ul style="list-style-type: none"> • In a less complex firm, the individual(s) <u>or individuals</u> assigned operational responsibility for the system of quality management may have a sufficient understanding of the firm and its engagements to undertake the risk assessment process. Furthermore, the documentation of the quality objectives, quality risks, and responses may be less extensive than for a more complex firm (e.g. for example, it may be documented in a single document). 	
<ul style="list-style-type: none"> • In a more complex firm, there may be a formal risk assessment process, involving multiple individuals and numerous activities. The process may be centralized (e.g. for example, the quality objectives, quality risks, and responses are established centrally for all business units, functions, and service lines) or decentralized (e.g. for example, the quality objectives, quality risks, and responses are established at a business unit, function, or service line level, with the outputs combined at the firm level). The firm’s network may also provide the firm with quality objectives, quality risks, and responses to be included in the firm’s system of quality management. 	
<p>A41. A40.—The process of establishing quality objectives, identifying and assessing quality risks, and designing and implementing responses is iterative, and the requirements of this ISQM<u>SQMS</u> are not intended to be addressed in a linear manner. For example <u>Examples of the iterative and nonlinear nature of the firm’s risk assessment process include the following:</u></p>	<p>To clarify</p>
<ul style="list-style-type: none"> • In identifying and assessing quality risks, the firm may<u>might</u> determine that an additional quality objective(s) needs to be established. 	<p>AICPA style</p>

<ul style="list-style-type: none"> When designing and implementing responses, the firm may<u>might</u> determine that a quality risk was not identified and assessed. 	AICPA style
<p>A42. A41.—Information sources that enable the firm to establish quality objectives, identify and assess quality risks, and design and implement responses form<u>are</u> part of the firm’s information and communication component and include <u>the following</u>:</p>	
<ul style="list-style-type: none"> The results of the firm’s monitoring and remediation process (see paragraphs 4243 and A174169). 	
<ul style="list-style-type: none"> Information from the network or service providers, including: 	
<ul style="list-style-type: none"> o information about network requirements or network services (see paragraph 4849); and 	
<ul style="list-style-type: none"> o other information from the network, including information about the results of monitoring activities undertaken by the network across the network firms (see paragraphs 50–51–52). 	
<p>Other information, both<u>whether</u> internal or external, may also be relevant to the firm’s risk assessment process, such as <u>the following</u>:</p>	To clarify
<ul style="list-style-type: none"> Information regarding complaints and allegations about failures to perform work in accordance with professional standards and applicable legal and regulatory requirements, or noncompliance with the firm’s policies or procedures established in accordance with this ISQM.<u>SQMS</u> 	
<ul style="list-style-type: none"> The results of external inspections. 	
<ul style="list-style-type: none"> Information from regulators about the entities for whom the firm performs engagements which<u>that</u> is made available to the firm, such as information from a securities regulator about an entity for whom the firm performs engagements (e.g. for example, irregularities in the entity’s financial statements or non-compliance with securities regulation<u>regulations</u>). 	
<ul style="list-style-type: none"> Changes in the system of quality management that affect other aspects of the system; for example, changes in the firm’s resources. 	
<ul style="list-style-type: none"> Other external sources, such as regulatory actions and litigation against the firm or other firms in the jurisdiction that may highlight areas for the firm to consider. 	

<i>Establish Quality Objectives (Ref: par. 2425)</i>	
A43. A42. —Law, regulation, or professional standards may establish requirements that give rise to additional quality objectives. For example, <u>if</u> a firm may be <u>is</u> required by law or regulation to appoint non-executive individuals to the firm’s governance structure and, the firm considers <u>may consider</u> it necessary to establish additional quality objectives to address the requirements.	
A44. A43. — <u>While</u> the nature and circumstances of the firm and its engagements may be <u>are specific to the firm, the quality objectives are sufficiently comprehensive</u> such that <u>it is unlikely that</u> the firm may not <u>would</u> find it necessary to establish additional quality objectives.	To be more emphatic
A45. A44. —The firm may establish sub-objectives to enhance the firm’s identification and assessment of quality risks, and design and implementation of responses.	
<i>Identify and Assess Quality Risks (Ref: par. 2526)</i>	
A46. A45. —There may be other conditions, events, circumstances, actions, or inactions not described in paragraph 25(26a) that may adversely affect the achievement of a quality objective.	
A47. A46. A risk arises from how, and the degree to which, a condition, event, circumstance, action, or inaction may adversely affect the achievement of a quality objective. Not all risks meet the definition of a <i>quality risk</i> . Professional judgment assists the firm in determining whether a risk is a quality risk, which is based on the firm’s consideration of whether there is a reasonable possibility of the risk occurring, and, individually, or in combination with other risks, adversely affecting the achievement of one or more quality objectives.	
A48. <u>Examples of the firm’s understanding of the conditions, events, circumstances, actions, or inactions that may adversely affect the achievement of the quality objectives and the related quality risks are as follows:</u>	AICPA style

Examples of the firm’s understanding of the conditions, events, circumstances, actions, or inactions that may adversely affect the achievement of the quality objectives	Examples of quality risks that may arise
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The strategic and operational decisions and actions, business processes, and business model of the firm: The firm’s overall financial goals are overly dependent on the extent of services provided by the firm not within the scope of this ~~ISQM~~SQMS.

In the context of governance and leadership, this may give rise to a number of quality risks such as the following:

- ~~Resources~~ are allocated or assigned in a manner that prioritizes the services not within the scope of this ~~ISQM~~SQMS and may negatively affect the quality of engagements within the scope of this ~~ISQM~~SQMS.
- ~~Decisions~~ about financial and operational priorities do not fully or adequately consider the importance of quality in ~~the performance~~

	<p>of performing engagements within the scope of this ISQM<u>SQMS</u>.</p>
<p>The characteristics and management style of leadership: The firm is a smaller firm with a few engagement partners with shared authority.</p>	<p>In the context of governance and leadership, this may give rise to a number of quality risks such as <u>the following</u>:</p> <ul style="list-style-type: none"> • Leadership's responsibilities and accountability for quality are not clearly defined and assigned. • The actions and behaviors of leadership that do not promote quality are not questioned.
<p>The complexity and operating characteristics of the firm: The firm has recently completed a merger with another firm.</p>	<p>In the context of resources, this may give rise to a number of quality risks, including <u>the following</u>:</p> <ul style="list-style-type: none"> •

	<p>Technological resources used by the two merged firms may be incompatible.</p> <ul style="list-style-type: none"> • Engagement teams may use intellectual resources developed by a firm prior to the merger, which are no longer consistent with the new methodology being used by the new merged firm.
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<p>A49. A47. Given the evolving nature of the system of quality management, the responses designed and implemented by the firm may give rise to conditions, events, circumstances, actions, or inactions that result in further quality risks. For example, the firm may implement a resource (e.g. for example, a technological resource) to address a quality risk, and quality risks may arise from the use of such resource.</p>	
<p>A50. A48. The degree to which a risk, individually, or in combination with other risks, may adversely affect the achievement of a quality objective(s) may vary based on the conditions, events, circumstances, actions, or inactions giving rise to the risk, taking <u>matters such as the following</u> into account, for example:</p>	

<ul style="list-style-type: none"> • How the condition, event, circumstance, action₂ or inaction would affect the achievement of the quality objective₂. 	
<ul style="list-style-type: none"> • How frequently the condition, event, circumstance, action₂ or inaction is expected to occur₂. 	
<ul style="list-style-type: none"> • How long it would take after the condition, event, circumstance, action₂ or inaction occurred for it to have an effect, and whether in that time the firm would have an opportunity to respond to mitigate the effect of the condition, event, circumstance, action₂ or inaction₂. 	
<ul style="list-style-type: none"> • How long the condition, event, circumstance, action₂ or inaction would affect the achievement of the quality objective once it has occurred₂. 	
<p>The assessment of quality risks need not comprise formal ratings or scores, although firms are not precluded from using them.</p>	
<p><i>Design and Implement Responses to Address the Quality Risks (Ref: par. 16(u), 26 17 and 27)</i></p>	
<p>A51. A49 The nature, timing₂ and extent of the responses are based on the reasons for the assessment given to the quality risks, which is the considered occurrence and effect on the achievement of one or more quality objectives.</p>	Deleted to clarify.
<p>A52. A50.—The responses designed and implemented by the firm may operate at the firm level or engagement level, or there may be a combination of responsibilities for actions to be taken at the firm and engagement level. <u>An</u> example of a response designed and implemented by the firm that operates at both the firm and engagement level <u>is as follows:</u></p>	
<p>The firm establishes policies or procedures for consultation₂ which include with whom consultation should be undertaken by engagement teams and the specific matters for which consultation is required. The firm appoints suitably qualified and experienced individuals to provide the consultations. The engagement team is responsible for identifying when matters for consultation occur and₂.</p>	

<p>initiating consultation, and implementing the conclusions from consultation.⁴⁰ <u>2</u></p>	
<p>A53. A51.—The need for formally documented policies or procedures may be greater for firms that have many personnel or that are geographically dispersed, in order to achieve consistency across the firm.</p>	
<p><i>Changes in the Nature and Circumstances of the Firm or Its Engagements (Ref: par. 2728)</i></p>	
<p>A54. A52.—<u>Examples of</u> scalability example to demonstrate how policies or procedures for identifying information about changes in the nature and circumstances of the firm and its engagements may vary <u>from other firms include the following:</u></p>	
<ul style="list-style-type: none"> • In a less complex firm, the firm may have informal policies or procedures to identify information about changes in the nature and circumstances of the firm or its engagements, particularly when the individual(s) <u>or individuals</u> responsible for establishing quality objectives, identifying and assessing quality risks, and designing and implementing responses is<u>are</u> able to identify such information in the normal course of their activities. 	
<ul style="list-style-type: none"> • In a more complex firm, the firm may need to establish more formal policies or procedures to identify and consider information about changes in the nature and circumstances of the firm or its engagements. This may include, for example, a periodic review of information relating to the nature and circumstances of the firm and its engagements, including ongoing tracking of trends and occurrences in the firm’s internal and external environment. 	
<p>A55. A53.—Additional quality objectives may need to be established, or quality risks and responses added to or modified, as part of the remedial actions undertaken by the firm to address an identified deficiency in accordance with paragraph 42<u>43</u>.</p>	
<p>A56. A54 The firm may have established quality objectives in addition to those specified by this ISQM<u>SQMS</u>. The firm may also identify information that indicates that additional quality objectives</p>	<p>AICPA style</p>

⁴⁰ ISA 220 (Revised), paragraphs 35

² [Paragraph 35 of SAS No. 146.](#)

<p>already<u>previously</u> established by the firm are no longer needed, or need to be modified.</p>	
<p>Governance and Leadership</p>	
<p><i>Commitment to Quality</i> (Ref: par. 28(a)<u>29a</u>)</p>	
<p>A57. A55 The firm’s culture is an important factor in influencing the behavior of personnel. Relevant ethical requirements ordinarily establish the principles of professional ethics, and are further addressed in the “<u>Relevant Ethical Requirements</u>-component” section of this ISQM<u>SQMS</u>. Professional values and attitudes may include <u>the following</u>:</p>	
<ul style="list-style-type: none"> • Professional manner; for example, timeliness, courteousness, respect, accountability, responsiveness, and dependability. 	
<ul style="list-style-type: none"> • A commitment to teamwork. 	
<ul style="list-style-type: none"> • Maintaining an open mind to new ideas or different perspectives in the professional environment. 	
<ul style="list-style-type: none"> • Pursuit of excellence. 	
<ul style="list-style-type: none"> • A commitment to continual improvement (e.g. for example, setting expectations beyond the minimum requirements and placing a focus on continual learning). 	
<ul style="list-style-type: none"> • Social responsibility. 	
<p>A58. A56.—The firm’s strategic decision-making process, including the establishment of a business strategy, may include matters such as the firm’s decisions about financial and operational matters, the firm’s financial goals, how financial resources are managed, growth of the firm’s market share, industry specialization, or new service offerings. The firm’s financial and operational priorities may directly or indirectly affect the firm’s commitment to quality, for example; the firm may have incentives that are focused on financial and operational priorities that may discourage behaviors that demonstrate a commitment to quality.</p>	
<p><i>Leadership</i> (Ref: par. 28(29b) and 28(29c))</p>	
<p>A59. A57.—The responses designed and implemented by the firm to hold leadership responsible and accountable for quality include the performance evaluations required by paragraph 56<u>57</u>.</p>	

<p>A60. A58.—Although leadership establishes the tone at the top through their<u>its</u> actions and behaviors, clear, consistent, and frequent actions and communications at all levels within the firm collectively contribute to the firm’s culture and demonstrates<u>demonstrate</u> a commitment to quality.</p>	
<p>Organizational Structure (Ref: par. 28<u>29d</u>)</p>	
<p>A61. A59.—The organizational structure of the firm may include operating units, operational processes, divisions, or geographical locations and other structures. In some instances, the firm may concentrate or centralize processes or activities in a service delivery center, and engagement teams may include personnel from the firm’s service delivery center who perform specific tasks that are repetitive or specialized in nature.</p>	
<p>Resources (Ref: par. 28<u>29e</u>)</p>	
<p>A62. A60.—The individual(s)<u>or individuals</u> assigned ultimate responsibility and accountability or operational responsibility for the system of quality management is<u>are</u>, in most cases, able to influence the nature and extent of resources that the firm obtains, develops, uses, and maintains, and how those resources are allocated or assigned, including the timing of when they are used.</p>	
<p>A63. A61.As<u>Because</u> resource needs may change over time, it may not be practicable to anticipate all resource needs. The firm’s resource planning may involve determining the resources currently required, forecasting the firm’s future resource needs, and establishing processes to deal with unanticipated resource needs when they arise.</p>	
<p>Relevant Ethical Requirements (Ref: par. 46(t), 29<u>17</u> and 30)</p>	
<p>A64. A62.—The IESBA<u>AICPA</u> code sets out the fundamental principles of ethics that establish<u>provide</u> the standards of behavior expected of a framework for the rules that govern the performance of professional accountant and establishes the International Independence Standards<u>responsibilities</u>. The fundamental principles are <u>responsibilities, the public interest,</u> integrity, objectivity, professional competence and <u>independence,</u> due care, confidentiality and scope and professional behavior. The IESBA<u>nature of services, Independence requirements are set forth in the “Independence Rule” (ET sec. 1.200.001) and related interpretations of the AICPA code also</u></p>	<p>Specific to ASB jurisdiction</p>

<p>specifies<u>and</u> the approach that a professional accountant is required to apply to comply with the fundamental principles<u>rules of state boards of accountancy</u> and, when applicable, the International Independence Standards. <u>regulatory agencies. Guidance on threats to independence and safeguards to mitigate such threats involving matters that are not explicitly addressed</u> in addition, the IESBA<u>AICPA</u> code addresses specific topics relevant to complying with the fundamental principles. <u>Law or regulation in a jurisdiction may also contain provisions addressing ethical requirements, including independence, such as privacy laws affecting the confidentiality of information.</u> are set forth in the “Conceptual Framework for Independence” (ET sec. 1.210.010).</p>	
<p>A65. A63 In some cases, the matters addressed by the firm in its system of quality management may be more specific than, or additional to, the provisions of relevant ethical requirements. Examples of matters that a firm may include in its system of quality management that are more specific than, or additional to, the provisions of relevant ethical requirements <u>include the following:</u></p>	
<ul style="list-style-type: none"> • The firm prohibits the acceptance of gifts and hospitality from a client, even if the value is trivial and inconsequential. 	
<ul style="list-style-type: none"> • The firm sets rotation periods for all engagement partners, including those performing other assurance or related services engagements, <u>and extends the rotation periods to all senior engagement team members.</u> attestation, review, and compilation engagements. 	
<p>A66. A64 Other components may affect or relate to the relevant ethical requirements component. Examples of relationships between the relevant ethical requirements component and other components <u>include the following:</u></p>	
<ul style="list-style-type: none"> • The information and communication component may address the communication of various matters related to relevant ethical requirements, including: 	
<ul style="list-style-type: none"> ○ the firm communicating the independence requirements to all personnel and others subject to independence requirements. 	
<ul style="list-style-type: none"> ○ personnel and engagement teams communicating relevant information to the firm without fear of reprisals, such as situations that may create threats to independence, or breaches of relevant ethical requirements. 	
<ul style="list-style-type: none"> • As part of the resources component, the firm may: 	

<ul style="list-style-type: none"> ○ assign individuals to manage and monitor compliance with relevant ethical requirements or to provide consultation on matters related to relevant ethical requirements. 	
<ul style="list-style-type: none"> ○ use IT applications to monitor compliance with relevant ethical requirements, including recording and maintaining information about independence. ○ — 	
<p>A67. A65. The relevant ethical requirements that apply to others depend on the provisions of the relevant ethical requirements and how the firm uses others in its system of quality management, or in the performance of performing engagements. Examples of relevant ethical requirements that apply to others <u>include the following:</u></p>	
<ul style="list-style-type: none"> • Relevant ethical requirements may include requirements for independence that apply to network firms or employees of network firms; for example, the IESBA <u>AICPA</u> code includes independence requirements that apply to network firms. 	
<ul style="list-style-type: none"> • Relevant ethical requirements may include a definition of <i>engagement team</i> or other similar concept, and the definition may include any individual who performs assurance procedures on the engagement (e.g., a component auditor or <u>for example,</u> a service provider engaged to attend a physical inventory count at a remote location). Accordingly, any requirements of the relevant ethical requirements that apply to the engagement team as defined in the relevant ethical requirements, or other similar concept, may also be relevant to such individuals. 	
<ul style="list-style-type: none"> • The principle of confidentiality may apply to the firm’s network, other network firms, or service providers, when they have access to client information obtained by the firm. 	
<p>Public Sector Considerations —</p>	
<p>A66. In achieving the quality objectives in this ISQM related to independence, public sector auditors may address independence in the context of the public sector mandate and statutory measures.</p>	<p>Not applicable in U.S.</p>
<p>A68. <u>AU-C section 600⁶ states that when the component auditor is not subject to the AICPA code, compliance with the ethics and independence requirements set forth in the International Ethics Standards Board for Accountants Code of Ethics for Professional</u></p>	<p>Specific to ASB jurisdiction</p>

⁶ Paragraph .A46 of AU-C section 600, *Special Considerations — Audits of Group Financial Statements (Including the Work of Component Auditors)*.

<p><u>Accountants is sufficient to fulfill the component auditor’s ethical responsibilities in the group audit.⁷ The firm may use, for example, confirmations, letters of representation, or other affirmations from network firms, employees of network firms, or service providers regarding the fulfillment of ethical requirements that are relevant to the firm.</u></p>	
<p>Acceptance and Continuance of Client Relationships and Specific Engagements</p>	
<p><i>The Nature and Circumstances of the Engagement and the Integrity and Ethical Values of the Client (Ref: par. 30(31a)(i))</i></p>	
<p>A69. A67. The information obtained about the nature and circumstances of the engagement may include <u>the following</u>:</p>	
<ul style="list-style-type: none"> • The industry of the entity for which the engagement is being undertaken and relevant regulatory factors; 	
<ul style="list-style-type: none"> • The nature of the entity; for example, its operations, organizational structure, ownership and governance, its business model, and how it is financed;and 	
<ul style="list-style-type: none"> • The nature of the underlying subject matter and the applicable criteria; for example, in the case of integrated<u>sustainability reporting</u>;and 	
<ul style="list-style-type: none"> ○ the underlying subject matter may include social, environmental, or health and safety information;and; 	
<ul style="list-style-type: none"> ○ the applicable criteria may be performance measures established by a recognized body of experts<u>specialists</u>. 	
<p>A70. A68 The information obtained to support the firm’s judgments about the integrity and ethical values of the client may include the identity and business reputation of the client’s principal owners, key management, and those charged with its governance.</p>	

⁷ [The section, “Application of the AICPA Code” \(ET sec. 0.200.020\), of the AICPA Code of Professional Conduct \(AICPA code\) explains that an AICPA member who is the group engagement partner will not be considered in violation of the AICPA code if a component auditor practicing outside the United States departs from the AICPA code with respect to the audit or review of group financial statements, as long as the component auditor’s conduct, at a minimum, is in accordance with the ethics and independence requirements set forth in the International Ethics Standards Board for Accountants’ Code of Ethics for Professional Accountants.](#)

<p>A71. Examples of factors that may affect the nature and extent of information obtained about the integrity and ethical values of the client <u>include the following:</u></p>	
<ul style="list-style-type: none"> • The nature of the entity for which the engagement is being performed, including the complexity of its ownership and management structure. 	
<ul style="list-style-type: none"> • The nature of the client’s operations, including its business practices. 	
<ul style="list-style-type: none"> • Information concerning the attitude of the client’s principal owners, key management, and those charged with its governance towards<u>toward</u> such matters as aggressive interpretation of accounting standards and the internal control environment. 	
<ul style="list-style-type: none"> • Whether the client is aggressively concerned with maintaining<u>keeping</u> the firm’s fees as low as possible. 	
<ul style="list-style-type: none"> • Indications of a client-imposed limitation in the scope of work. 	
<ul style="list-style-type: none"> • Indications that the client might be involved in money laundering or other criminal activities. 	
<ul style="list-style-type: none"> • The reasons for the proposed appointment of the firm and non-reappointment of the previous firm. 	
<ul style="list-style-type: none"> • The identity and business reputation of related parties. 	
<p>A72. A69. The firm may obtain the information from a variety of internal and external sources, including <u>the following:</u></p>	
<ul style="list-style-type: none"> • In the case of an existing client, information from current or previous engagements, if applicable, or inquiry of other personnel who have performed other engagements for the client. 	
<ul style="list-style-type: none"> • In the case of a new client, inquiry of existing or previous providers of professional accountancy<u>auditing</u> services to the client, in accordance with relevant ethical requirements. 	
<ul style="list-style-type: none"> • Discussions with other third parties, such as bankers, legal counsel, and industry peers. 	
<ul style="list-style-type: none"> • Background searches of relevant databases (which may be intellectual resources). In some cases, the firm may use a service provider to perform the background search. 	

<p>A73. A70.—Information that is obtained during the firm’s acceptance and continuance process <u>also</u> may often also be relevant to the engagement team when planning and performing the engagement. Professional standards may specifically require the engagement team to obtain or consider such information. For example, ISA 220 (Revised)⁴¹<u>SAS No. 146</u>⁸ requires the engagement partner to take into account information obtained in the acceptance and continuance process in planning and performing the audit engagement.</p>	
<p>A74. A71.—Professional standards or applicable legal and regulatory requirements may include specific provisions that need to be addressed before accepting or continuing a client relationship or specific engagement and may also require the firm to make inquiries of an existing or predecessor firm when accepting an engagement. For example, when there has been a change of auditors, ISA 300⁴²<u>AU-C section 210, Terms of Engagement</u>,⁹ requires the auditor, prior to starting an initial audit, to communicate with<u>request management to authorize</u> the predecessor auditor in compliance with relevant ethical requirements<u>to respond fully to the auditor’s inquiries regarding matters that will assist the auditor in determining whether to accept the engagement</u>. The IESBA<u>“Conflicts of Interest for Members in Public Practice” interpretation of the AICPA</u> code also includes requirements for the<u>addresses</u> consideration of conflicts of interests<u>interest</u> in accepting or continuing a client relationship or specific engagement and communication with the existing or predecessor firm when accepting an engagement that is an audit or review of financial statements<u>(ET sec. 1.110.010)</u>.</p>	<p>Specific to ASB jurisdiction</p>
<p><i>The Firm’s Ability to Perform the EngagementEngagements</i> (Ref: par. 30(31a)(ii))</p>	
<p>A75. A72.—The firm’s ability to perform the engagement in accordance with professional standards and applicable legal and regulatory requirements may be affected by <u>the following</u>:</p>	
<ul style="list-style-type: none"> • The availability of appropriate resources to perform the engagement; 	
<ul style="list-style-type: none"> • Having access to information to perform the engagement; or to the persons who provide such information; and 	

⁴¹ISA 220 (Revised),⁸ Paragraph 23 of SAS No. 146.

⁴²ISA 300, *Planning an Audit of Financial Statements*, paragraph 13(b)

⁹ Paragraph .11 of AU-C section 210, *Terms of Engagement*.

<ul style="list-style-type: none"> Whether the firm and the engagement team are able to fulfill their responsibilities in relation to the relevant ethical requirements. 	
<p>A76. Examples of factors the firm may consider in determining whether appropriate resources are available to perform the engagement <u>include the following:</u></p>	
<ul style="list-style-type: none"> The circumstances of the engagement and the reporting deadline. 	
<ul style="list-style-type: none"> The availability of individuals with the appropriate competence and capabilities, including sufficient time, to perform the engagement. This includes having: <ul style="list-style-type: none"> individuals to take overall responsibility for directing and supervising the engagement; individuals with knowledge of the relevant industry or the underlying subject matter or criteria to be applied in the preparation of the subject matter information and experience with relevant regulatory or reporting requirements; and individuals to perform audit procedures on the financial information of a component for purposes of an audit of group financial statements. 	
<ul style="list-style-type: none"> The availability of expertsspecialists, if needed. 	
<ul style="list-style-type: none"> If an engagement quality review is needed, whether there is an individual available who meets the eligibility requirements in ISQMSQMS No. 2. 	
<ul style="list-style-type: none"> The need for technological resources; for example, IT applications that enable the engagement team to perform procedures on the entity’s data. 	
<ul style="list-style-type: none"> The need for intellectual resources; for example, a methodology, industry or subject -matter -specific guides, or access to information sources. 	
<p><i>The Firm’s Financial and Operational Priorities (Ref: par. 30(31b))</i></p>	
<p>A77. A73.—Financial priorities may focus on the profitability of the firm, and fees obtained for the performance ofperforming engagements have an effect on the firm’s financial resources. Operational priorities may include strategic focus areas, such as growth of the firm’s market share, industry specialization, or new service offerings. There may be circumstances when<u>in which</u> the firm is satisfied with the fee quoted</p>	

<p>for an engagement, but it is not appropriate for the firm to accept or continue the engagement or client relationship (e.g. for example, when the client lacks integrity and ethical values).</p>	
<p>A78. A74.—There may be other circumstances when<u>in which</u> the fee quoted for an engagement is not sufficient given the nature and circumstances of the engagement, and it may diminish the firm’s ability to perform the engagement in accordance with professional standards and applicable legal and regulatory requirements. The IESBA<u>“Fees and Other Types of Remuneration” rule of the AICPA</u> code addresses fees and other types of remuneration, including circumstances that may create a threat to compliance with the fundamental principle of professional competence and due care if the fee quoted for an engagement is too low (ET section 1.500).</p>	<p>Specific to U.S.</p>
<p>Engagement Performance</p>	
<p><i>Responsibilities of the Engagement Team and Direction, Supervision, and Review (Ref: par. 34(32a) and 34(32b))</i></p>	
<p>A79. A75.—Professional standards or applicable legal and regulatory requirements may include specific provisions regarding the overall responsibility of the engagement partner. For example, ISA 220 (Revised)<u>SAS No. 146</u> deals with the overall responsibility of the engagement partner for managing and achieving quality on the engagement and for being sufficiently and appropriately involved throughout the engagement, including having<u>taking</u> responsibility for appropriate direction and supervision of the engagement team and review of their<u>its</u> work.</p>	
<p>A80. A76.—Examples of direction, supervision, and review <u>include the following:</u></p>	
<ul style="list-style-type: none"> • Direction and supervision of the engagement team may include: 	
<ul style="list-style-type: none"> <ul style="list-style-type: none"> ○ tracking the progress of the engagement; 	
<ul style="list-style-type: none"> <ul style="list-style-type: none"> ○ considering the following with respect to members of the engagement team: 	
<ul style="list-style-type: none"> <ul style="list-style-type: none"> <ul style="list-style-type: none"> ▪ Whether they understand their instructions; and 	
<ul style="list-style-type: none"> <ul style="list-style-type: none"> <ul style="list-style-type: none"> ▪ Whether the work is being carried out in accordance with the planned approach to the engagement; 	

<ul style="list-style-type: none"> ▪ addressing matters arising during the engagement, considering their significance₂ and modifying the planned approach appropriately₇; and 	
<ul style="list-style-type: none"> ▪ identifying matters for consultation or consideration by more experienced engagement team members during the engagement. 	
<ul style="list-style-type: none"> • A review of work performed may include considering whether₇: 	
<ul style="list-style-type: none"> ○ the work has been performed in accordance with the firm’s policies or procedures, professional standards₂ and applicable legal and regulatory requirements; 	
<ul style="list-style-type: none"> ○ significant matters have been raised for further consideration; 	
<ul style="list-style-type: none"> ○ appropriate consultations have been undertaken₂ and the resulting conclusions have been documented and implemented; 	
<ul style="list-style-type: none"> ○ there is a need to revise the nature, timing₂ and extent of planned work; 	
<ul style="list-style-type: none"> ○ the work performed supports the conclusions reached and is appropriately documented; 	
<ul style="list-style-type: none"> ○ the evidence obtained for an assurance engagement is sufficient and appropriate to support the report; and 	
<ul style="list-style-type: none"> ○ the objectives of the engagement procedures have been achieved. 	
<p>A81. A77.—In some circumstances, the firm may use personnel from a service delivery center in the firm or individuals from a service delivery center in another network firm to perform procedures on the engagement (i.e. that is, the personnel or other individuals are included in the engagement team). In such circumstances, the firm’s policies or procedures may specifically address the direction and supervision of the individuals and review of their work, such as₇:</p>	
<ul style="list-style-type: none"> • what aspects of the engagement may be assigned to individuals in the service delivery center; 	
<ul style="list-style-type: none"> • how the engagement partner, or their designee, is expected to direct, supervise₂ and review the work undertaken by individuals in the service delivery center; and 	
<ul style="list-style-type: none"> • the protocols for communication between the engagement team and individuals in the service delivery center. 	
<p><i>Professional Judgment and Professional Skepticism (Ref: par. 34(32c))</i></p>	

<p>A82. A78. Professional skepticism supports the quality of judgments made on an assurance engagement and, through these judgments, the overall effectiveness of the engagement team in performing the assurance engagement. Other pronouncements of the IAASB <u>professional standards</u> may address the exercise of professional judgment or <u>maintenance of professional skepticism</u> at the engagement level. For example, ISA 220 (Revised)¹³ <u>SAS No. 146</u>¹⁰ provides examples of impediments to the exercise <u>maintenance</u> of professional skepticism at the engagement level, unconscious auditor biases that may impede the exercise <u>maintenance</u> of professional skepticism, and possible actions that the engagement team may take to mitigate such impediments.</p>	<p>ASB preferred wording</p>
<p>Consultation (Ref: par. 31(32d))</p>	
<p>A83. A79. Consultation typically involves a discussion at the appropriate professional level, with individuals within or outside the firm who have specialized expertise, on difficult or contentious matters. An environment that reinforces the importance and benefit of consultation and encourages engagement teams to consult may contribute to supporting a culture that demonstrates a commitment to quality.</p>	
<p>A84. A80. Difficult or contentious matters on which consultation is needed may either be specified by the firm, or the engagement team may identify matters that require consultation. The firm may also specify how conclusions are to <u>should</u> be agreed <u>upon</u> and implemented.</p>	
<p>A85. A81 <u>SAS No. ISA 220 (Revised)</u>¹⁴ <u>146</u>¹¹ includes requirements for the engagement partner related to consultation.</p>	
<p>Differences of Opinion (Ref: par. 31(32e))</p>	
<p>A86. A82. The firm may encourage that <u>identifying</u> differences of opinion are identified at an early stage, and may specify the steps to be taken in raising and dealing with them, including how the matter is to be resolved and how the related conclusions should be implemented and documented. In some circumstances, resolving differences of opinion</p>	<p>AICPA style</p>

¹³ ISA 220 (Revised), paragraphs A34–A36

¹⁰ Paragraphs A34–A36 of SAS No. 146.

¹⁴ ISA 220 (Revised), paragraph 35

¹¹ Paragraph 35 of SAS No. 146.

<p>may be achieved through consulting with another practitioner or firm, or a professional or regulatory body.</p>	
<p>Engagement Documentation (Ref: par. 31(32f))</p>	
<p>A87. A83.—Law, regulation, or professional standards may prescribe the time limits by which the assembly of final engagement files for specific types of engagements are to be completed. Where<u>When</u> no such time limits are prescribed in law or regulation, the time limit may be determined by the firm. <u>For example,</u> in the case of engagements conducted under<u>in accordance with</u> the ISAs<u>SSAEs</u> or ISAEs<u>SSARSS</u>, an appropriate time limit within which to complete the assembly of the final engagement file is ordinarily not more than 60 days after the date of the engagement report.</p>	<p>Specific to U.S.</p>
<p>A88. A84.—The retention and maintenance of engagement documentation may include managing the safe custody, integrity, accessibility, or retrievability of the underlying data and the related technology. The retention and maintenance of engagement documentation may involve the use of IT applications. The integrity of engagement documentation may be compromised if it is altered, supplemented, or deleted without authorization to do so, or if it is permanently lost or damaged.</p>	
<p>A89. A85.—Law, regulation, or professional standards may prescribe the retention periods for engagement documentation. If the retention periods are not prescribed, the firm may consider the nature of the engagements performed by the firm and the firm’s circumstances, including whether the engagement documentation is needed to provide a record of matters of continuing significance to future engagements. In the case of engagements conducted under <u>generally accepted auditing standards or</u> the ISAs or ISAEs<u>SSAEs</u>, the retention period is ordinarily no shorter than five years from the date of the engagement report, or, if later, the date of the auditor’s report on the group financial statements, when applicable.</p>	
<p>Resources (Ref: par. 3233)</p>	
<p>A90. A86.—Resources for the purposes of the resources component include <u>the following</u>:</p>	
<ul style="list-style-type: none"> • Human resources. 	
<ul style="list-style-type: none"> • Technological resources; for example, IT applications. 	

<ul style="list-style-type: none"> • Intellectual resources; for example, written policies or procedures, a methodology, or guides. 	
<p>Financial resources are also relevant to the system of quality management because they are necessary for obtaining, developing, and maintaining the firm’s human resources, technological resources, and intellectual resources. Given that the management and allocation of financial resources is strongly influenced by leadership, the quality objectives in governance and leadership, such as those that address financial and operational priorities, address financial resources.</p>	
<p>A91. A87.—Resources may be internal to the firm, or may be obtained externally from the firm’s network, another network firm, or service provider. Resources may be used in performing activities within the firm’s system of quality management, or in the performance of performing engagements as part of operating the system of quality management. In circumstances when <u>in which</u> a resource is obtained from the firm’s network or another network firm, paragraphs 4849–5253 form part of the responses designed and implemented by the firm in achieving the objectives in this component.</p>	
<p><i>Human Resources</i></p>	
<p><i>Hiring, Developing, and Retaining Personnel and Personnel Competence and Capabilities</i> (Ref: par. 32(a), 32(33a and d))</p>	
<p>A92. A88. <i>Competence</i> is the ability of the individual to perform a role and goes beyond knowledge of principles, standards, concepts, facts, and procedures; it is the integration and application of technical competence, professional skills, and professional ethics, values, and attitudes. Competence can be developed through a variety of methods, including professional education, continuing professional development, training, work experience, or coaching of less experienced engagement team members by more experienced engagement team members.</p>	
<p>A93. A89. Law, regulation, or professional standards may establish requirements addressing competence and capabilities, such as. <u>For example, law or regulation may establish</u> requirements for the professional licensing of engagement partners, including requirements regarding their professional education and continuing professional development.</p>	<p>To clarify</p>
<p>Examples of policies or procedures relating to hiring, developing and retaining personnel</p>	

<p>A94. A90.—The policies or procedures designed and implemented by the firm relating to hiring, developing, and retaining personnel may address, <u>for example, the following</u>:</p>	
<ul style="list-style-type: none"> • Recruiting individuals who have, or are able to develop, appropriate competence. 	
<ul style="list-style-type: none"> • Training programs focused on developing the competence of personnel and continuing professional development. 	
<ul style="list-style-type: none"> • Evaluation mechanisms that are undertaken at appropriate intervals and include competency areas and other performance measures. 	
<ul style="list-style-type: none"> • Compensation, promotion, and other incentives, for all personnel, including engagement partners and individuals assigned roles and responsibilities related to the firm’s system of quality management. 	
<p><i>Personnel’s Commitment to Quality and Accountability and Recognition for Commitment to Quality (Ref: par. 32(33b))</i></p>	
<p>A95. A91.—Timely evaluations and feedback help support and promote the continual development of the competence of personnel. Less formal methods of evaluation and feedback may be used, such as in the case of firms with fewer personnel.</p>	
<p>A96. A92.—Positive actions or behaviors demonstrated by personnel may be recognized through various means, such as through compensation, promotion, or other incentives. In some circumstances, simple or informal incentives that are not based on monetary rewards may be appropriate.</p>	
<p>A97. A93.—The manner in which the firm holds personnel accountable for actions or behaviors that negatively affect quality, such as failing to demonstrate a commitment to quality, develop and maintain the competence to perform their role, or implement the firm’s responses as designed, may depend on the nature of the action or behavior, including its severity and frequency of occurrence. <u>The following are some</u> actions the firm may take when personnel demonstrate actions or behaviors that negatively affect quality may include:</p>	
<ul style="list-style-type: none"> • • Training or other professional development. 	
<ul style="list-style-type: none"> • • Considering the effect of the matter on the evaluation, compensation, promotion, or other incentives of those involved. 	

<ul style="list-style-type: none"> • Disciplinary action, if appropriate. 	
<p>Individuals Obtained From External Sources (Ref: par. 32(33c))</p>	
<p>A98. A94. Professional standards may include responsibilities for the engagement partner regarding the appropriateness of resources. For example, ISA 220 (Revised)¹⁵ <u>SAS No. 146</u>¹² addresses the responsibility of the engagement partner for determining that sufficient and appropriate resources to perform the engagement are assigned or made available to the engagement team in a timely manner in accordance with the firm’s policies or procedures.</p>	
<p><i>Engagement Team Members Assigned to Each Engagement</i> (Ref: par. 32(33d))</p>	
<p>A99. A95. Engagement team members may be assigned to engagements by:</p>	
<ul style="list-style-type: none"> • the firm, including assigning personnel from a service delivery center in the firm. 	
<ul style="list-style-type: none"> • the firm’s network or another network firm when the firm uses individuals from the firm’s network or another network firm to perform procedures on the engagement (e.g. for example, a component auditor or a service delivery center of the network or another network firm). 	
<ul style="list-style-type: none"> • a service provider when the firm uses individuals from a service provider to perform procedures on the engagement (e.g. for example, a component auditor from a firm that is not within the firm’s network). 	
<p>A100. A96 <u>SAS No. 146</u>¹³ —ISA 220 (Revised)¹⁶ addresses the responsibility of the engagement partner to determine that members of the engagement team, and any auditor’s external experts <u>specialists</u> and internal auditors who provide direct assistance (who are not part of the engagement team), collectively have the appropriate competence and capabilities, including sufficient time, to perform the engagement. ISA</p>	<p>Moved to par. A14</p>

¹⁵ ~~ISA 220 (Revised), paragraph 25~~

¹² Paragraph 25 of SAS No. 146.

¹⁶ ~~ISA 220 (Revised), paragraph 26~~

¹³ Paragraph 26 of SAS No. 146.

<p>600¹⁷ expands on how ISA 220 (Revised) is to be applied in relation to an audit of group financial statements. The responses designed and implemented by the firm to address the competence and capabilities of engagement team members assigned to the engagement may include policies or procedures that address the following:</p>	
<ul style="list-style-type: none"> • Information that may be obtained by the engagement partner and factors to consider in determining that the engagement team members assigned to the engagement, including those assigned by the firm’s network, another network firm, or service provider, have the competence and capabilities to perform the engagement. 	
<ul style="list-style-type: none"> • How concerns about the competence and capabilities of engagement team members, in particular those assigned by the firm’s network, another network firm, or service provider, may be resolved. 	
<p>A101. A97.—The requirements in paragraphs 4849–5253 are also applicable when using individuals from the firm’s network or another network firm on an engagement, including component auditors (see, for example, paragraph A479190).</p>	
<p>Technological Resources (Ref: par. 3233f)</p>	
<p>A102. A98.—Technological resources, which are typically IT applications, form part of the firm’s IT environment. The firm’s IT environment also includes the supporting IT infrastructure and the IT processes and human resources involved in those processes:</p>	
<ul style="list-style-type: none"> • An IT application is a program or a set of programs that is designed to perform a specific function directly for the user or, in some cases, for another application program. 	
<ul style="list-style-type: none"> • The IT infrastructure is comprised ofcomprises the IT network, operating systems, and databases and their related hardware and software. 	
<ul style="list-style-type: none"> • The IT processes are the firm’s processes to manage access to the IT environment, manage program changes or changes to the IT environment, and manage IT operations, which includes monitoring the IT environment. 	

¹⁷ ISA 600, *Special Considerations—Audits of Group Financial Statements (Including the Work of Component Auditors)*, paragraph 19

<p>A103. A99.—A technological resource may serve multiple purposes within the firm, and some of the purposes may be unrelated to the system of quality management. Technological resources that are relevant for the purposes of this ISQM<u>SQMS</u> are <u>as follows</u>:</p>	
<ul style="list-style-type: none"> • Technological resources that are directly used in designing, implementing, or operating the firm’s system of quality management; 	
<ul style="list-style-type: none"> • Technological resources that are used directly by engagement teams in the performance of<u>performing</u> engagements; and 	AICPA style
<ul style="list-style-type: none"> • Technological resources that are essential to enabling the effective operation of the above<u>preceding</u>, such as, in relation to an IT application, the IT infrastructure and IT processes supporting the IT application. 	AICPA style
<p>A104. <u>Examples of</u> scalability examples to demonstrate how the technological resources that are relevant for the purposes of this ISQM<u>SQMS</u> may differ in <u>in firms of different complexity include the following</u>:</p>	To clarify
<ul style="list-style-type: none"> • <u>In</u> a less complex firm, the technological resources may comprise a commercial IT application used by engagement teams, which that has been purchased from a service provider. The IT processes that support the operation of the IT application may also be relevant, although they may be simple (e.g. for <u>example</u>, processes for authorizing access to the IT application and processing updates to the IT application). 	
<ul style="list-style-type: none"> • In a more complex firm, the technological resources may be more complex and may comprise <u>the following</u>: 	
<ul style="list-style-type: none"> ○ Multiple IT applications, including custom developed applications or applications developed by the firm’s network, such as: 	
<ul style="list-style-type: none"> ▪ IT applications used by engagement teams (e.g. for <u>example</u>, engagement software and automated audit tools); and 	
<ul style="list-style-type: none"> ▪ IT applications developed and used by the firm to manage aspects of the system of quality management (e.g. for <u>example</u>, IT applications to monitor independence or assign personnel to engagements); 	

<ul style="list-style-type: none"> ○ The IT processes that support the operation of these IT applications, including the individuals responsible for managing the IT infrastructure and IT processes and the firm’s processes for managing program changes to the IT applications. 	
<p>A105. A100. The firm may consider the following matters in obtaining, developing, implementing, and maintaining an IT application:</p>	
<ul style="list-style-type: none"> • The data inputs are complete and appropriate; 	
<ul style="list-style-type: none"> • Confidentiality of the data is preserved; 	
<ul style="list-style-type: none"> • The IT application operates as designed and achieves the purpose for which it is intended; 	
<ul style="list-style-type: none"> • The outputs of the IT application achieve the purpose for which they will be used; 	
<ul style="list-style-type: none"> • The general IT controls necessary to support the IT application’s continued operation as designed are appropriate; 	
<ul style="list-style-type: none"> • The need for specialized skills to utilize use the IT application effectively, including the training of individuals who will use the IT application; and 	
<ul style="list-style-type: none"> • The need to develop procedures that set out how the IT application operates. 	
<p>A106. A101. The firm may specifically prohibit the use of IT applications or features of IT applications until such time that it has been determined that they operate appropriately and have been approved for use by the firm. Alternatively, the firm may establish policies or procedures to address circumstances when <u>in which</u> the engagement team uses an IT application that is not approved by the firm. Such policies or procedures may require the engagement team to determine that the IT application is appropriate for use prior to using it on the engagement, through considering the matters in paragraph A100 <u>102</u>. ISA 220 (Revised)¹⁸ <u>SAS No. 146</u>¹⁴ addresses the engagement partner’s responsibilities for engagement resources.</p>	

¹⁸ ~~ISA 220 (Revised), paragraphs 25–28~~

¹⁴ Paragraphs 25–28 of SAS No. 146.

<p><i>Intellectual Resources (Ref: par. 32(33g))</i></p>	
<p>A107. A102. Intellectual resources include the information <u>and materials</u> the firm uses to enable the operation of the system of quality management and promote consistency in the performance of performing engagements. Examples of intellectual resources <u>include</u> written policies or procedures, a methodology, industry or subject <u>-matter-specific guides, accounting guides, standardized documentation,</u> or access to information sources (e.g. for example, subscriptions to websites that provide in-depth information about entities or other information that is typically used in the performance of performing engagements).</p>	
<p>A108. A103. Intellectual resources may be made available through technological resources; <u>for example,</u> the firm’s methodology may be embedded in the IT application that facilitates the planning and performance of the engagement.</p>	
<p><i>Use of Technological and Intellectual Resources (Ref: par. 32(33f)–32(g))</i></p>	
<p>A109. A104. The firm may establish policies or procedures regarding the use of the firm’s technological and intellectual resources. <u>Examples of</u> such policies or procedures may include the following:</p>	
<ul style="list-style-type: none"> • Require<u>Requiring</u> the use of certain IT applications or intellectual resources in the performance of performing engagements, or relating to other aspects of the engagement, such as in archiving the engagement file. 	
<ul style="list-style-type: none"> • Specify<u>Specifying</u> the qualifications or experience that individuals need to use the resource, including the need for an expert<u>a specialist</u> or training; <u>for example,</u> the firm may specify the qualifications or expertise needed to use an IT application that analyzes data, given that specialized skills may be needed to interpret the results. 	
<ul style="list-style-type: none"> • Specify<u>Specifying</u> the responsibilities of the engagement partner regarding the use of technological and intellectual resources. 	
<ul style="list-style-type: none"> • Set<u>Setting</u> out how the technological or intellectual resources are to be used, including how individuals should interact with an IT application or how the intellectual resource should be applied, 	

and the availability of support or assistance in using the technological or intellectual resource-	
Service Providers (Ref: par. 16(v), 32(17 and 33h))	
A105.	
A110. In some circumstances, the firm may use resources that are provided by a service provider, particularly in circumstances when <u>in which</u> the firm does not have access to the appropriate resources internally. Notwithstanding that a firm may use resources from a service provider, the firm remains responsible for its system of quality management.	
<i>Examples of resources from a service provider</i>	
A111. <u>Examples of resources from a service provider include the following:</u>	
<ul style="list-style-type: none"> • Individuals engaged to perform the firm’s monitoring activities or engagement quality reviews, or to provide consultation on technical matters- 	
<ul style="list-style-type: none"> • A commercial IT application used to perform audit engagements- 	
<ul style="list-style-type: none"> • Individuals performing procedures on the firm’s engagements; for example, component auditors from other firms not within the firm’s network or individuals engaged to attend a physical inventory count at a remote location- 	
<ul style="list-style-type: none"> • An auditor’s external expert <u>specialist</u> used by the firm to assist the engagement team in obtaining audit evidence- 	
A112. A106. In identifying and assessing quality risks, the firm is required to obtain an understanding of the conditions, events, circumstances, actions, or inactions that may adversely affect the achievement of the quality objectives, which includes conditions, events, circumstances, actions, or inactions relating to service providers. In doing so, the firm may consider the nature of the resources provided by service providers, how and the extent to which they will be used by the firm, and the general characteristics of the service providers used by the firm (e.g. for example , the varying types of other professional services firms that are used), in order to identify and assess quality risks related to the use of such resources.	
A113. A107. In determining whether a resource from a service provider is appropriate for use in the firm’s system of quality	

<p>management or in the performance of<u>performing</u> engagements, the firm may obtain information about the service provider and the resource they provide<u>it provides</u> from a number of sources. <u>The following are</u> matters the firm may consider include:</p>	
<ul style="list-style-type: none"> • The related quality objective and quality risks. For example, in the case of a methodology from a service provider, there may be quality risks related to the quality objective in paragraph 32<u>(33g)</u>, such as a quality risk that the service provider does not update the methodology to reflect changes in professional standards and applicable legal and regulatory requirements. 	
<ul style="list-style-type: none"> • The nature and scope of the resources, and the conditions of the service (e.g. for example, in relation to an IT application, how often updates will be provided, limitations on the use of the IT application, and how the service provider addresses confidentiality of data). 	
<ul style="list-style-type: none"> • The extent to which the resource is used across the firm, how the resource will be used by the firm, and whether it is suitable for that purpose. 	
<ul style="list-style-type: none"> • The extent of customization of the resource for the firm. 	
<ul style="list-style-type: none"> • The firm’s previous use of the service provider. 	
<ul style="list-style-type: none"> • The service provider’s experience in the industry and reputation in the market. 	
<ul style="list-style-type: none"> • <u>The results of attestation engagements performed by independent third parties on the resource (for example, assurance engagements on quality control materials or reports on service organization controls).</u> 	Additional guidance
<p>A114. A108.–The firm may have a responsibility to take further actions in using the resource from a service provider so that the resource functions effectively. For example, the firm may need to communicate information to the service provider in order for the resource to function effectively, or, in relation to an IT application, the firm may need to have supporting IT infrastructure and IT processes in place.</p>	
<p>A115. <u>The evaluation of a service provider from a firm not within the firm’s network that is used as a component auditor may be different than that of a service provider engaged directly by the firm. For example, in understanding the competency of the component auditor to perform the engagement, it may not be necessary or practicable for</u></p>	Additional guidance

<p><u>the firm to obtain an understanding of how the component auditor updates its methodology to reflect changes in professional standards. Rather, the firm could perform procedures such as review of results of regulatory inspections, transparency or audit quality information published by the component auditor’s firm, or evaluation of the reputation of the component auditor.</u></p>	
<p>Information and Communication (Ref: par. 33<u>34</u>)</p>	
<p>A116. A109. Obtaining, generating, or communicating information is generally an ongoing process that involves all personnel and encompasses the dissemination of information within the firm and externally. Information and communication is<u>are</u> pervasive to all components of the system of quality management.</p>	
<p>The Firm’s Information System (Ref: par. 33(a)<u>34a</u>)</p>	
<p>A117.A110 Reliable and relevant information includes information that is accurate, complete, timely, and valid to enable the proper functioning of the firm’s system of quality management and to support decisions regarding the system of quality management.</p>	
<p>A118. A111. The information system may include the use of manual or IT elements, which affect the manner in which information is identified, captured, processed, maintained, and communicated. The procedures to identify, capture, process, maintain, and communicate information may be enforced through IT applications, and in some cases may be embedded within the firm’s responses for other components. In addition, digital records may replace or supplement physical records.</p>	
<p>A119. <u>An example of scalability</u> example to demonstrate how the information system may be designed in a less complex firm<u>is that</u> less complex firms with fewer personnel and direct involvement of leadership may not need rigorous policies and procedures that specify how information should be identified, captured, processed, and maintained.</p>	
<p>Communication Within the Firm (Ref: par. 33(b), 33<u>34b-c</u>)</p>	
<p>A120. A112. The firm may recognize and reinforce the responsibility of personnel and engagement teams to exchange</p>	

<p>information with the firm and with one another by establishing communication channels to facilitate communication across the firm. Examples of communication among the firm, personnel and engagement teams, <u>and other individuals include the following:</u></p>	
<ul style="list-style-type: none"> • The firm communicates the responsibility for implementing the firm’s responses to personnel and engagement teams. 	
<ul style="list-style-type: none"> • The firm communicates changes to the system of quality management to personnel and engagement teams, to the extent that the changes are relevant to their responsibilities and enables personnel and engagement teams to take prompt and appropriate action in accordance with their responsibilities. 	
<ul style="list-style-type: none"> • The firm communicates information that is obtained during the firm’s acceptance and continuance process that is relevant to engagement teams in planning and performing engagements. 	
<ul style="list-style-type: none"> • Engagement teams communicate to the firm <u>following</u> information about <u>to the firm:</u> 	
<ul style="list-style-type: none"> ○ <u>Information about</u> the client that is obtained during the performance of an engagement that may have caused the firm to decline the client relationship or specific engagement had that information been known prior to accepting or continuing the client relationship or specific engagement. 	
<ul style="list-style-type: none"> ○ <u>Information about</u> the operation of the firm’s responses (e.g. for example, concerns about the firm’s processes for assigning personnel to engagements), which, in some cases, may indicate a deficiency in the firm’s system of quality management. 	
<ul style="list-style-type: none"> • Engagement teams communicate information to the engagement quality reviewer or individuals providing consultation. 	
<ul style="list-style-type: none"> • Group engagement teams communicate matters to component auditors in accordance with the firm’s policies or procedures, including matters related to quality management at the engagement level. 	
<ul style="list-style-type: none"> • The individual(s) <u>or individuals</u> assigned operational responsibility for compliance with independence requirements communicates <u>communicate</u> to relevant personnel and engagement teams changes in the independence requirements and the firm’s policies or procedures to address such changes. 	

<p><i>Communication With External Parties</i></p>	
<p><i>Communication to or Within the Firm’s Network and to Service Providers</i> (Ref: par. 33<u>34</u>d)(i))</p>	
<p>A121. A113. In addition to the firm communicating information to or within the firm’s network or to a service provider, the firm may need to obtain information from the network, a network firm₂ or a service provider that supports the firm in the design, implementation₂ and operation of its system of quality management. For example-of information obtained by₂ the firm from within the firm’s network The firm obtains <u>may obtain</u> information from the network or other network firms about clients of other network firms, where <u>when</u> there are independence requirements that affect the firm.</p>	
<p><i>Communication With Others External to the Firm</i> (Ref: par. 33<u>34</u>d)(ii))</p>	
<p>A122. A114. Examples of when law, regulation₃ or professional standards may require the firm to communicate information to external parties <u>include the following:</u></p>	
<ul style="list-style-type: none"> • The firm becomes aware of non-compliance with laws and regulations by a client, and relevant ethical requirements require the firm to report the non-compliance with laws and regulations to an appropriate authority outside the client entity₇ or to consider whether such reporting is an appropriate action in the circumstances. 	
<ul style="list-style-type: none"> • Law or regulation requires the firm to publish a transparency report and specifies the nature of the information that is required to be included in the transparency report. 	
<ul style="list-style-type: none"> • Securities law or regulation requires the firm to communicate certain matters to those charged with governance. 	
<p><u>Paragraphs A131–A135 address communications to support external parties’ understanding of the system of quality management beyond those required by law, regulation, or professional standards.</u></p>	<p>Additional guidance</p>
<p>A123. A115. In some cases, law or regulation may preclude the firm from communicating information related to its system of quality management externally. Examples of when the firm may be precluded from communicating information externally <u>include the following:</u></p>	

<ul style="list-style-type: none"> • Privacy or secrecy<u>Confidentiality</u> law or regulation prohibits disclosure of certain information. 	
<ul style="list-style-type: none"> • Law, regulation, or relevant ethical requirements include provisions addressing the duty of confidentiality. 	
<p>Specified Responses (Ref: par. 34 <u>35</u>)</p>	
<p>A124. A116The specified responses may address multiple quality risks related to more than one quality objective across different components. For example, policies or procedures for complaints and allegations may address quality risks related to quality objectives in resources (e.g. for example, personnel’s commitment to quality), relevant ethical requirements, and governance and leadership. The specified responses alone are not sufficient to achieve the objectives of the system of quality management.</p>	<p>Moved to paragraph 35 as essential guidance</p>
<p>Relevant Ethical Requirements (Ref: par. 34(a) <u>35(a-b)</u>)</p>	
<p>A125. A117Relevant ethical requirements may contain provisions regarding the identification and evaluation of threats and how they are <u>should</u> be addressed. For example, the IESBA<u>AICPA</u> code provides a conceptual framework for this purpose and, in applying the conceptual framework, requires that the firm use the reasonable and informed third party test.</p>	
<p>A126. A118Relevant ethical requirements may specify how the firm is required to respond to a breach. For example, the IESBA Code sets out requirements for the firm in the event“<u>Breach of an Independence interpretation (ET sec. 1.298.010)</u>” of a breach of the IESBA Code and includes specific requirements“<u>Independence Rule” (ET sec. 1.200.001)</u> <u>contains guidance</u> addressing breaches of the International Standards, which includes requirements for communication with external parties<u>interpretation of the AICPA code, which also contains guidance</u> addressing a breach of any other provision of the <u>AICPA code</u>.</p>	<p>Specific for ASB jurisdiction</p>
<p>A127. A119Matters the firm may address relating to breaches of the relevant ethical requirements include <u>the following</u>:</p>	
<ul style="list-style-type: none"> • The communication of breaches of the relevant ethical requirements to appropriate personnel; 	

<ul style="list-style-type: none"> • The evaluation of the significance of a breach and its effect on compliance with relevant ethical requirements; 	
<ul style="list-style-type: none"> • The actions to be taken to satisfactorily address the consequences of a breach, including that such actions be taken as soon as practicable; 	
<ul style="list-style-type: none"> • Determining whether to report a breach to external parties, such as those charged with governance of the entity to which the breach relates or an external oversight authority; and 	
<ul style="list-style-type: none"> • Determining the appropriate actions to be taken in relation to the individual(s) <u>or individuals</u> responsible for the breach. 	
<p><i>Complaints and Allegations (Ref: par. 34(<u>35c</u>)</i></p>	
<p>A128. A120. Establishing policies or procedures for dealing with complaints and allegations may assist the firm in preventing engagement reports from being issued that are inappropriate. It also may assist the firm in:</p>	
<ul style="list-style-type: none"> • identifying and dealing with individuals, including leadership, who do not act or behave in a manner that demonstrates a commitment to quality and supports the firm’s commitment to quality; or 	
<ul style="list-style-type: none"> • identifying deficiencies in the system of quality management. 	
<p>A129. A121. Complaints and allegations may be made by personnel, or others external to the firm (e.g. for example, clients, component auditors, or individuals within the firm’s network).</p>	
<p><i>Information That Becomes Known Subsequent to Accepting or Continuing a Client Relationship or Specific Engagement (Ref: par. 34(<u>35d</u>)</i></p>	
<p>A130. A122.—Information that becomes known subsequent to accepting or continuing a client relationship or specific engagement may:</p>	
<ul style="list-style-type: none"> • have existed at the time of the firm’s decision to accept or continue the client relationship or specific engagement, and the firm was not aware of such information; or 	
<ul style="list-style-type: none"> • relate to new information that has arisen since the decision to accept or continue the client relationship or specific engagement. 	

<p>A131. Examples of matters addressed in the firm’s policies or procedures for circumstances when<u>in which</u> information becomes known subsequent to accepting or continuing a client relationship or specific engagement that may have affected the firm’s decision to accept or continue a client relationship or specific engagement <u>include the following:</u></p>	
<ul style="list-style-type: none"> • Undertaking consultation within the firm or with legal counsel. 	
<ul style="list-style-type: none"> • Considering whether there is a professional, legal, or regulatory requirement for the firm to continue the engagement. 	
<ul style="list-style-type: none"> • Discussing with the appropriate level of the client’s management and with those charged with governance or the engaging party the action that the firm might take based on the relevant facts and circumstances. 	
<ul style="list-style-type: none"> • When it is determined that withdrawal is an appropriate action: 	
<ul style="list-style-type: none"> <ul style="list-style-type: none"> ○ Informing the client’s management and those charged with governance or the engaging party of this decision and the reasons for the withdrawal. 	
<ul style="list-style-type: none"> <ul style="list-style-type: none"> ○ Considering whether there is a professional, legal, or regulatory requirement for the firm to report the withdrawal from the engagement, or from both the engagement and the client relationship, together with the reasons for the withdrawal, to regulatory authorities. 	
<p>A132. A123. In some circumstances, jurisdictional law or regulation may impose an obligation on the firm to accept or continue a client engagement, or in the case of the public sector, the firm may be appointed through statutory provisions.</p>	<p>Not relevant in U.S.</p>
<p>A133. Example<u>Examples</u> of matters addressed in the firm’s policies or procedures in circumstances when<u>in which</u> the firm is obligated to accept or continue an engagement or the firm is unable to withdraw from an engagement, and the firm is aware of information that would have caused the firm to decline or discontinue the engagement <u>, include the following:</u></p>	
<ul style="list-style-type: none"> • The firm considers the effect of the information on the performance of the engagement. 	
<ul style="list-style-type: none"> • The firm communicates the information to the engagement partner, and requests the engagement partner to increase the 	

<p>extent and frequency of the direction and supervision of the engagement team members and review of their work.</p>	
<ul style="list-style-type: none"> • The firm assigns more experienced personnel to the engagement. 	
<ul style="list-style-type: none"> • The firm determines that an engagement quality review should be performed. 	
<p>Communication With External Parties (Ref. Para: par: 34(35e))</p>	
<p>A134.A124. The firm’s ability to maintain stakeholder confidence in the quality of its engagements may be enhanced through relevant, reliable, and transparent communication by the firm about the activities that it has undertaken to address quality, and the effectiveness of those activities.</p>	
<p>A135.A125. External parties who may use information about the firm’s system of quality management, and the extent of their interest in the firm’s system of quality management, may vary based on the nature and circumstances of the firm and its engagements.</p>	
<p><i>Examples of external parties who may use information about the firm’s system of quality management</i></p>	
<p>A136. <u>Examples of external parties who may use information about the firm’s system of quality management include the following:</u></p>	
<ul style="list-style-type: none"> • Management or those charged with governance of the firm’s clients may use the information to determine whether to appoint the firm to perform an engagement. 	
<ul style="list-style-type: none"> • External oversight authorities may have indicated a desire for the information to support their responsibilities in monitoring the quality of engagements across a jurisdiction and in understanding the work of firms. 	
<ul style="list-style-type: none"> • Other firms who use the work of the firm in the performance of performing engagements (e.g. for example, in relation to a group audit) may have requested such information. 	
<ul style="list-style-type: none"> • Other users of the firm’s engagement reports, such as investors who use engagement reports in their decision making, may have indicated a desire for the information. 	
<p>A137. A126.—The information about the system of quality management provided to external parties, including information communicated to those charged with governance about how the system</p>	

<p>of quality management supports the consistent performance of quality engagements, may address such matters as <u>the following</u>:</p>	
<ul style="list-style-type: none"> • The nature and circumstances of the firm, such as the organizational structure, business model, strategy, and operating environment. 	
<ul style="list-style-type: none"> • The firm’s governance and leadership, such as <ul style="list-style-type: none"> ○ its culture; ○ how it demonstrates a commitment to quality; and assigned ○ <u>how</u> roles, responsibilities, and authority with respect to the system of quality management are assigned 	
<ul style="list-style-type: none"> • How the firm fulfills its responsibilities in accordance with relevant ethical requirements, including those related to independence. 	
<ul style="list-style-type: none"> • Factors that contribute to quality engagements; for example, such information may be presented in the form of engagement quality indicators with narrative to explain the indicators. 	
<ul style="list-style-type: none"> • The results of the firm’s monitoring activities and external inspections, and how the firm has remediated identified deficiencies or is otherwise responding to them. 	
<ul style="list-style-type: none"> • The evaluation undertaken in accordance with paragraphs 53–54–55 of whether the system of quality management provides the firm with reasonable assurance that the objectives of the system are being achieved and the conclusion thereon, including the basis for the judgments made in undertaking—the evaluation<u>evaluating</u> and concluding. 	
<ul style="list-style-type: none"> • How the firm has responded to emerging developments and changes in the circumstances of the firm or its engagements, including how the system of quality management has been adapted to respond to such changes. 	
<ul style="list-style-type: none"> • The relationship between the firm and the network, the overall structure of the network, a description of network requirements and network services, the responsibilities of the firm and the network (including that the firm is ultimately responsible for the system of quality management), and information about the overall scope and results of network monitoring activities across the network firms. 	
<p>Communication with Those Charged with Governance (Ref. Para: 34(e)(i))</p>	

A127. How the communication with those charged with governance is undertaken (i.e., by the firm or the engagement team) may depend on the firm's policies or procedures and the circumstances of the engagement.	See paragraphs 138-141
A128. ISA 260 (Revised) deals with the auditor's responsibility to communicate with those charged with governance in an audit of financial statements, and addresses the auditor's determination of the appropriate person(s) within the entity's governance structure with whom to communicate¹⁹ and the communication process.²⁰ In some circumstances, it may be appropriate to communicate with those charged with governance of entities other than listed entities (or when performing other	
<u>Determining When It Is Appropriate to Communicate With External Parties (Ref: par. 35e(i))</u>	
A138. <u>The firm's determination of when it is appropriate to communicate with external parties about the firm's system of quality management is a matter of professional judgment and may be influenced by matters such as the following:</u>	Moved from ISQM 1 par. A128-A130 and expanded
<ul style="list-style-type: none"> • <u>The types of engagements performed by the firm</u> 	
<ul style="list-style-type: none"> • <u>The types of entities for which such engagements), are undertaken;</u> for example, entities that may have public interest or public accountability characteristics, such as: <ul style="list-style-type: none"> ○ entities that hold a significant amount of assets in a fiduciary capacity for a large number of stakeholders, including financial institutions, such as certain banks, insurance companies, and pension funds;<u>;</u> ○ entities with a high public profile; or whose management or owners have a high public profile; <u>and</u> ○ entities with a large number and wide range of stakeholders. 	

¹⁹ ~~ISA 260 (Revised), Communication with Those Charged with Governance, paragraphs 11–13~~

²⁰ ~~ISA 260 (Revised), paragraphs 18–22~~

<p>Public sector considerations</p> <p>A129. The firm may determine it is appropriate to communicate to those charged with governance of a public sector entity about how the firm's system of quality management supports the consistent performance of quality engagements, taking into account the size and complexity of the public sector entity, the range of its stakeholders, the nature of the services it provides, and the role and responsibilities of those charged with governance.</p>	<p>Not relevant in U.S.</p>
<p>Determining When it is Otherwise Appropriate to Communicate with External Parties (Ref. Para: 34(e)(ii))</p> <p>A130. The firm's determination of when it is appropriate to communicate with external parties about the firm's system of quality management is a matter of professional judgment and may be influenced by matters such as:</p> <p>□ The types of engagements performed by the firm, and the types of entities for which such engagements are undertaken.</p>	<p>See par. A140</p>
<ul style="list-style-type: none"> • The nature and circumstances of the firm. 	
<ul style="list-style-type: none"> • The nature of the firm's operating environment, such as customary business practice in the firm's jurisdiction and the characteristics of the financial markets in which the firm operates. 	
<ul style="list-style-type: none"> • The extent to which the firm has already communicated with external parties in accordance with law or regulation (i.e. that is, whether further communication is needed, and, if so, the matters to be communicated). 	
<ul style="list-style-type: none"> • The expectations of stakeholders in the firm's jurisdiction, including the understanding and interest that external parties have expressed about the engagements undertaken by the firm, and the firm's processes in performing the engagements. 	
<ul style="list-style-type: none"> • Jurisdictional trends. 	
<ul style="list-style-type: none"> • The information that is already available to external parties. 	
<ul style="list-style-type: none"> • How external parties may use the information, and their general understanding of matters related to firms' system<u>systems</u> of quality management and audits or reviews of financial statements, or other assurance or related services engagements. <u>performed by the firm in its accounting and auditing practice</u> 	
<ul style="list-style-type: none"> • The public interest benefits of external communication and whether it would reasonably be expected to outweigh the costs (monetary or otherwise) of such communication. 	

<p>The above<u>preceding</u> matters may also affect the information provided by the firm in the communication, and the nature, timing, and extent and appropriate form of communication.</p>	
<p>A139. <u>AU-C section 260, <i>The Auditor’s Communication With Those Charged With Governance</i>, deals with the auditor’s responsibility to communicate with those charged with governance in an audit of financial statements and addresses the auditor’s determination of the appropriate person or persons within the entity’s governance structure with whom to communicate¹⁵ and the communication process.¹⁶ In some circumstances, it may be appropriate to include information about the firm’s system of quality management in those communications with those charged with governance (or when performing other engagements, for example, review or examination engagements). How the communication with those charged with governance is undertaken (that is, by the firm or the engagement team) may depend on the firm’s policies or procedures and the circumstances of the engagement.</u></p>	<p>Additional guidance</p>
<p><u>Considerations for Engagements for Governmental Organizations</u></p>	
<p>A140. <u>The firm may determine it is appropriate to communicate to those charged with governance of a governmental organization about how the firm’s system of quality management supports the consistent performance of quality engagements, taking into account the size and complexity of the governmental organization, the range of its stakeholders, the nature of the services it provides, and the roles and responsibilities of those charged with governance.</u></p>	<p>See ISQM 1 par. 130</p>
<p><i>Nature, Timing, and Extent and Appropriate Form of Communication With External Parties</i> (Ref. Para: <u>par:</u></p>	
<p>34(35e)(iii))</p>	
<p>A141. A131. The firm may consider the following attributes in preparing information that is communicated to external parties:</p>	
<ul style="list-style-type: none"> • The information is specific to the circumstances of the firm. Relating the matters in the firm’s communication directly to the specific circumstances of the firm may help to minimize the 	

¹⁵ Paragraphs .07–.09 of AU-C section 260, *The Auditor’s Communication With Those Charged With Governance*.

¹⁶ Paragraphs .15–.20 of AU-C section 260.

<p>potential that such information becomes overly standardized and less useful over time.</p>	
<ul style="list-style-type: none"> • The information is presented in a clear and understandable manner, and the manner of presentation is neither misleading nor would inappropriately influence the users of the communication (e.g. for example, the information is presented in a manner that is appropriately balanced towards positive and negative aspects of the matter being communicated). 	
<ul style="list-style-type: none"> • The information is accurate and complete in all material respects and does not contain information that is misleading. 	
<ul style="list-style-type: none"> • The information takes into consideration the information needs of the users for whom it is intended. In considering the information needs of the users, the firm may consider matters such as the level of detail that users would find meaningful and whether users have access to relevant information through other sources (e.g. for example, the firm’s website). 	
<p>A142. A132. The firm uses professional judgment in determining, in the circumstances, the appropriate form of communication with the external party, including communication with those charged with governance when performing an audit of financial statements of listed entities, which may be made orally or in writing. Accordingly, the form of communication may vary.</p>	
<p>Examples of formforms of communication to external parties <u>include the following</u>:</p>	
<ul style="list-style-type: none"> • A publication such as a transparency report or audit quality report. 	
<ul style="list-style-type: none"> • Targeted written communication to specific stakeholders (e.g. for example, information about the results of the firm’s monitoring and remediation process). 	
<ul style="list-style-type: none"> • Direct conversations and interactions with the external party (e.g. for example, discussions between the engagement team and those charged with governance). 	
<ul style="list-style-type: none"> • A webpage.web page 	
<ul style="list-style-type: none"> • Other forms of digital media, such as social media, or interviews or presentations via webcast or video. 	

<i>Engagements Subject to an Engagement Quality Review</i>	
<i>Engagement Quality Review Required by Law or Regulation</i> (Ref: par. 34(35f)(iii))	
A143. A133. Law or regulation may require an engagement quality review to be performed, for example, for audit engagements for entities that:	
<ul style="list-style-type: none"> are <i>public interest entities</i> as defined in a particular jurisdiction; 	
<ul style="list-style-type: none"> Operate in the public sector or which are <u>governmental organizations or</u> recipients of government funding, or entities with public accountability; 	
<ul style="list-style-type: none"> operate in certain industries (e.g. for example, financial institutions such as banks, insurance companies, and pension funds); 	
<ul style="list-style-type: none"> meet a specified asset threshold; or 	
<ul style="list-style-type: none"> are under the management of a court or judicial process (e.g. for example, liquidation). 	
<i>Engagement Quality Review as a Response to Address One or More Quality Risk(s) Risks</i> (Ref: par. 34(35f)(iii))	
A144. A134. The firm’s understanding of the conditions, events, circumstances, actions, or inactions that may adversely affect the achievement of the quality objectives, as required by paragraph 25(26a) (ii), relates to the nature and circumstances of the engagements performed by the firm. In designing and implementing responses to address one or more quality risk(s) risks, the firm may determine that an engagement quality review is an appropriate response based on the reasons for the assessments given to the quality risks.	
A145. <u>Criteria established by the firm to determine whether an engagement quality review is an appropriate response for one or more quality risks may relate to the types of engagements performed by the firm and reports to be issued, and the types of entities for which engagements are undertaken.</u> Examples of conditions, events, circumstances, actions, or inactions giving rise to one or more such quality risk(s) for which an engagement quality review may be an appropriate response risks include the following:	Expanded guidance

Those relating to the types of engagements performed by the firm and reports to be issued:	
<ul style="list-style-type: none"> • Engagements that involve a high level of complexity or judgment, such as the following: 	
<ul style="list-style-type: none"> ○ Audits of financial statements for entities operating in an industry that typically has accounting estimates with a high degree of estimation uncertainty (e.g. for example, certain large financial institutions or mining entities), or for entities for which uncertainties exist related to events or conditions that may cast significant doubt on their ability to continue as a going concern. 	
<ul style="list-style-type: none"> ○ Assurance engagements that require specialized skills and knowledge in measuring or evaluating the underlying subject matter against the applicable criteria (e.g. for example, a greenhouse gas statement in which there are significant uncertainties associated with the quantities reported therein). 	
<ul style="list-style-type: none"> • Engagements on which issues have been encountered, such as audit engagements with recurring internal or external inspection findings, unremediated significant deficiencies in internal control, or a material restatement of comparative information in the financial statements. 	
<ul style="list-style-type: none"> • Engagements for which unusual circumstances have been identified during the firm’s acceptance and continuance process (e.g. for example, a new client that had a disagreement with its previous auditor or assurance practitioner). 	
<ul style="list-style-type: none"> • Engagements that involve reporting on financial or non-financial information that is expected to be included in a regulatory filing, and that may involve a higher degree of judgment, such as pro forma financial information to be included in a prospectus. 	
Those relating to the types of entities for which engagements are undertaken:	
<ul style="list-style-type: none"> • Entities in emerging industries, or for which the firm has no previous experience. 	
<ul style="list-style-type: none"> • Entities for which concerns were expressed in communications from securities or prudential regulators. 	
<ul style="list-style-type: none"> • Entities other than listed Entities that may have public interest or public accountability characteristics, for example such as the following: 	
<ul style="list-style-type: none"> ○ Entities that hold a significant amount of assets in a fiduciary 	

<p>capacity for a large number of stakeholders, including financial institutions, such as certain banks, insurance companies, and pension funds for which an engagement quality review is not otherwise required by law or regulation.</p>	
<ul style="list-style-type: none"> ○ Entities with a high public profile, or whose management or owners have a high public profile. 	
<ul style="list-style-type: none"> ○ Entities with a large number and wide range of stakeholders. 	
<ul style="list-style-type: none"> ○ <u>Governmental organizations</u> 	
<ul style="list-style-type: none"> ▪ <u>Due to their size and complexity, the range of their stakeholders or the nature of the services they provide</u> ▪ <u>Due to the complexity, and importance to users, of additional reporting requirements established by law or regulation (for example, a separate report on instances of noncompliance with law or regulation to the legislature or other governing body or communicating such instances in the auditor’s report on the financial statements)</u> 	<p>Additional guidance</p>
<p>A146. A135.—The firm’s responses to address quality risks may include other forms of engagement reviews that are not an engagement quality review. For example, for audits of financial statements, the firm’s responses may include reviews of the engagement team’s procedures relating to significant risks, or reviews of certain significant judgments, by personnel who have specialized technical expertise. In some cases, these other types of engagement reviews may be undertaken in addition to an engagement quality review.</p>	
<p>A147.A136.—In some cases, the firm may determine that there are no audits or other engagements for which an engagement quality review or another form of engagement review is an appropriate response to address the quality risk(s) <u>risks</u>.</p>	
<p>Public sector considerations</p>	
<p>A137. The nature and circumstances of public sector entities (e.g., due to their size and complexity, the range of their stakeholders, or the nature of the services they provide) may give rise to quality risks. In these circumstances, the firm may determine that an engagement quality review is an appropriate response to address such quality risks. Law or regulation may establish additional reporting requirements for the auditors of public sector entities (e.g., a separate report on instances of noncompliance with law or regulation to the legislature or other</p>	<p>Not relevant to ASB jurisdiction</p>

<p>governing body or communicating such instances in the auditor's report on the financial statements). In such cases, the firm may also consider the complexity of such reporting, and its importance to users, in determining whether an engagement quality review is an appropriate response.</p>	
<p>Monitoring and Remediation Process (Ref: par. 3536-4748)</p>	
<p>A148. A138. In addition to enabling the evaluation of the system of quality management, the monitoring and remediation process facilitates the proactive and continual improvement of engagement quality and the system of quality management. For example <u>Examples follow:</u></p>	
<ul style="list-style-type: none"> Given the inherent limitations of a system of quality management, the firm's identification of deficiencies is not unusual, and it is an important aspect of the system of quality management, because prompt identification of deficiencies enables the firm to remediate them in a timely and effective manner, and contributes to a culture of continual improvement. 	
<ul style="list-style-type: none"> The monitoring activities may provide information that enables the firm to prevent a deficiency through responding to a finding that could, over a period of time, lead to a deficiency. 	
<p>Designing and Performing Monitoring Activities (Ref: par. 37-38-39)</p>	
<p>A149. A139. The firm's monitoring activities may comprise a combination of ongoing monitoring activities and periodic monitoring activities. Ongoing monitoring activities are generally routine activities, built into the firm's processes and performed on a real-time basis, reacting to changing conditions. Periodic monitoring activities are conducted at certain intervals by the firm. In most cases, ongoing monitoring activities provide information about the system of quality management in a timelier manner.</p>	
<p>A150. A140. Monitoring activities may include the inspection of in-process engagements. Inspections of engagements are designed to monitor that <u>whether</u> an aspect of the system of quality management is designed, implemented, and operating in the manner intended. In some circumstances, the system of quality management may include responses that are designed to review engagements while they are in the process of being performed that appear similar in nature to an inspection of in-process engagements (e.g. for example, reviews that are designed to detect failures or shortcomings in the system of quality management so that they can prevent a quality risk from occurring).</p>	

<p>The purpose of the activity will guide<u>drives</u> its design and implementation, and where it fits within the system of quality management (i.e. that is, whether it is an inspection of an in-process engagement that is a monitoring activity or a review of an engagement that is a response to address a quality risk).</p>	
<p>A151. A141. The nature, timing, and extent of the monitoring activities may also be affected by other matters, including:</p>	
<ul style="list-style-type: none"> • the size, structure, and organization of the firm, 	
<ul style="list-style-type: none"> • the involvement of the firm’s network in monitoring activities, and 	
<ul style="list-style-type: none"> • the resources that the firm intends to use to enable monitoring activities, such as the use of IT applications. 	
<p>A152. A142. When performing monitoring activities, the firm may determine that changes to the nature, timing, and extent of the monitoring activities are needed, such as when findings indicate the need for more extensive monitoring activities.</p>	
<p><i>The Design of the Firm’s Risk Assessment Process and Monitoring and Remediation Process (Ref: par. 37(<u>38c</u>))</i></p>	
<p>A153. A143. How the firm’s risk assessment process is designed (e.g. for example, a centralized or decentralized process, or the frequency of review) may affect the nature, timing, and extent of the monitoring activities, including monitoring activities over the firm’s risk assessment process.</p>	
<p>A154. A144. How the firm’s monitoring and remediation process is designed (i.e. that is, the nature, timing, and extent of the monitoring and remediation activities, taking into account the nature and circumstances of the firm) may affect the monitoring activities undertaken by the firm to determine whether the monitoring and remediation process is achieving the intended purpose as described in paragraph 35<u>36</u>.</p>	
<p>A155. <u>An example of scalability</u> example to demonstrate <u>how</u> the monitoring activities for the monitoring and remediation process <u>may differ in firms of different complexity is as follows:</u></p>	
<ul style="list-style-type: none"> • In a less complex firm, the monitoring activities may be simple, since <u>because</u> information about the monitoring and remediation process may be readily available in the form of leadership’s knowledge, 	

<p>based on their frequent interaction with the system of quality management, of the nature, timing, and extent of the monitoring activities undertaken, the results of the monitoring activities, and the firm’s actions to address the results.</p>	
<ul style="list-style-type: none"> • In a more complex firm, the monitoring activities for the monitoring and remediation process may be specifically designed to determine that the monitoring and remediation process is providing relevant, reliable, and timely information about the system of quality management, and responding appropriately to identified deficiencies. 	
<p><i>Changes in the System of Quality Management</i> (Ref: par. 37(38d))</p>	
<p>A156. A145. Changes in the system of quality management may include:</p>	
<ul style="list-style-type: none"> • changes to address an identified deficiency in the system of quality management, and 	
<ul style="list-style-type: none"> • changes to the quality objectives, quality risks, or responses as a result of changes in the nature and circumstances of the firm and its engagements. 	
<p>When changes occur, previous monitoring activities undertaken by the firm may no longer provide the firm with information to support the evaluation of the system of quality management and, therefore, the firm’s monitoring activities may include monitoring of those areas of change.</p>	
<p><i>Previous Monitoring Activities</i> (Ref: par. 37(e)38e and 44b)</p>	
<p>A157. A146. The results of the firm’s previous monitoring activities may indicate areas of the system where a deficiency may arise, particularly areas where there is a history of identified deficiencies.</p>	
<p>A158. A147. Previous monitoring activities undertaken by the firm may no longer provide the firm with information to support the evaluation of the system, including on areas of the system of quality management that have not changed, particularly when time has elapsed since the monitoring activities were undertaken.</p>	

<i>Other Relevant Information</i> (Ref: par. 37(17 and 38f))	
A159. A148. In addition to the sources of information indicated in paragraph 37(38f) , other relevant information may include <u>the following</u> :	
<ul style="list-style-type: none"> • Information communicated by the firm’s network in accordance with paragraphs 50(51c) and 54(52b) about the firm’s system of quality management, including the network requirements or network services that the firm has included in its system of quality management. 	
<ul style="list-style-type: none"> • Information communicated by a service provider about the resources the firm uses in its system of quality management. 	
<ul style="list-style-type: none"> • Information from regulators about the entities for whom the firm performs engagements, which is made available to the firm, such as information from a securities regulator about an entity for whom the firm performs engagements (e.g. for example, irregularities in the entity’s financial statements). 	
A160. A149. The results of external inspections or other relevant information, both internal and external, may indicate that previous monitoring activities undertaken by the firm failed to identify a deficiency in the system of quality management. This information may affect the firm’s consideration of the nature, timing, and extent of the monitoring activities.	
A161. A150. External inspections are not a substitute for the firm’s internal monitoring activities. Nevertheless, the results of external inspections inform the nature, timing, and extent of the monitoring activities.	
<i>Engagement Inspections</i> (Ref: par. 38 <u>39</u>)	
A162. A151 Examples of matters in paragraph 37 <u>38</u> that may be considered by the firm in selecting completed engagements for inspection <u>include the following</u> :	
<ul style="list-style-type: none"> • In relation to the conditions, events, circumstances, actions, or inactions giving rise to the quality risks: <ul style="list-style-type: none"> ○ The types of engagements performed by the firm, and the extent of the firm’s experience in performing the type of engagement. 	

<ul style="list-style-type: none"> ○ The types of entities for which engagements are undertaken, for example <u>such as the following</u>: 	
<ul style="list-style-type: none"> □ Entities that are listed. 	
<ul style="list-style-type: none"> ▪ Entities operating in emerging industries. 	
<ul style="list-style-type: none"> ▪ Entities operating in industries associated with a high level of complexity or judgment. 	
<ul style="list-style-type: none"> ▪ Entities operating in an industry that is new to the firm. 	
<ul style="list-style-type: none"> ▪ The tenure and experience of engagement partners. 	
<ul style="list-style-type: none"> ● The results of previous inspections of completed engagements, including for each engagement partner. 	
<ul style="list-style-type: none"> ● In relation to other relevant information: 	
<ul style="list-style-type: none"> ▪ Complaints or allegations about an engagement partner. 	
<ul style="list-style-type: none"> ▪ The results of external inspections, including for each engagement partner. 	
<ul style="list-style-type: none"> ▪ The results of the firm’s evaluation of each engagement partner’s commitment to quality. 	
<p>A163. A152. The firm may undertake multiple monitoring activities, other than inspection of completed engagements, that focus on determining whether engagements have complied with policies or procedures. These monitoring activities may be undertaken on certain engagements or engagement partners. The nature and extent of these monitoring activities, and the results, may be used by the firm in determining <u>the following</u>:</p>	
<ul style="list-style-type: none"> ● <u>How often to select completed engagements for inspection, and</u> which completed engagements to select for inspection; <u>based on the factors described in paragraph A159</u> 	
<ul style="list-style-type: none"> ● <u>Which engagement partners to select for inspection;</u> <u>and</u> how frequently to select an engagement partner for inspection; or; <u>based on factors such as how long it has been since the engagement partner was subject to inspection, the results of previous inspections of the engagement partner, or the engagement partner’s experience with performing engagements</u> 	

<p><u>at different levels of service, in new industries, or with complex financial reporting matters</u></p>	
<ul style="list-style-type: none"> • Which aspects of the engagement to consider when performing the inspection of completed engagements- 	
<p><u>For example, if the firm has undertaken inspections of in-process engagements,</u></p>	<p>Expanded guidance (not intended to create a difference in application between ISQM 1 and SQMS No, 1)</p>
<ul style="list-style-type: none"> • <u>the firm may determine it appropriate to reduce the extent of selection of completed engagements for inspection;</u> 	
<ul style="list-style-type: none"> • <u>the results of the inspections of in-process engagements may indicate areas of risk that may affect which completed engagements are selected for inspection; or</u> 	
<ul style="list-style-type: none"> • <u>the results of the inspections of in-process engagements may identify negative quality issues that prompt the firm to shorten the inspection cycle or expand the extent of completed engagement inspections.</u> 	
<p>A164. A153.—The inspection of completed engagements for engagement partners on a cyclical basis may assist the firm in monitoring whether engagement partners have fulfilled their overall responsibility for managing and achieving quality on the engagements <u>to which</u> they are assigned to.</p>	
<p>A165. Example <u>Examples</u> of how <u>policies and procedures that</u> a firm may <u>establish to</u> apply a cyclical basis for the inspection of completed engagements for each engagement partner <u>include</u> the firm may establish <u>following</u> policies or procedures addressing the inspection of completed engagements that:</p>	<p>Revised wording to clarify</p>
<ul style="list-style-type: none"> • set forth the standard period of the inspection cycle, such as the inspection of a completed engagement for each engagement partner performing audits of financial statements once every, <u>for example,</u> three years, and for all other engagement partners, once every, <u>for example,</u> five years;. 	
<ul style="list-style-type: none"> • set out the criteria for selecting completed engagements, including that for an engagement partner performing audits of financial statements, the engagement(s) <u>engagements</u> selected include an audit engagement;. 	
<ul style="list-style-type: none"> • address selecting <u>the selection of</u> engagement partners in a manner that is unpredictable; and. 	

<ul style="list-style-type: none"> • address when it is necessary or appropriate to select engagement partners more, or less, frequently than the standard period set out in the policy, for example. <u>Examples follow</u>: 	
<ul style="list-style-type: none"> ○ The firm may select engagement partners more frequently than the standard period set out in the firm’s policy when <u>the following apply</u>: 	
<ul style="list-style-type: none"> ○ Multiple deficiencies have been identified by the firm that have been evaluated as severe, and the firm determines that a more frequent cyclical inspection is needed across all engagement partners. 	
<ul style="list-style-type: none"> ○ The engagement partner performs engagements for entities operating in a certain industry wherein <u>in which</u> there are high levels of complexity or judgment. 	
<ul style="list-style-type: none"> ○ An engagement performed by the engagement partner has been subject to other monitoring activities, and the results of the other monitoring activities were unsatisfactory. 	
<ul style="list-style-type: none"> ○ The engagement partner has performed an engagement for an entity operating in an industry in which the engagement partner has limited experience. 	
<ul style="list-style-type: none"> ○ <u>The engagement partner has limited experience in performing that level of service engagements</u> 	Additional guidance
<ul style="list-style-type: none"> ○ The engagement partner is a newly appointed engagement partner, or has recently joined the firm from another firm or another jurisdiction. 	
<ul style="list-style-type: none"> • The firm may defer the selection of the engagement partner (e.g. <u>for example</u>, deferring for a year beyond the standard period set out in the firm’s policy) when: 	
<ul style="list-style-type: none"> ○ engagements performed by the engagement partner have been subject to other monitoring activities during the standard period set out in the firm’s policy, and 	
<ul style="list-style-type: none"> ○ the results of the other monitoring activities provide sufficient information about the engagement partner (i.e., <u>that is,</u> performing the inspection of completed engagements would unlikely provide the firm with further information about the engagement partner). 	
<p>A166. A154 The matters considered in an inspection of an engagement depend on how the inspection will be used to monitor the</p>	

<p>system of quality management. Ordinarily, the inspection of an engagement includes determining that responses that are implemented at the engagement level (e.g. for example, the firm’s policies and procedures in respect of engagement performance); have been implemented as designed and are operating effectively.</p>	
<p><u>The Relationship of Peer Review to Monitoring</u></p>	
<p>A167. <u>A peer review is not a substitute for all monitoring activities. However, because the objective of a peer review is similar to that of an inspection, the firm’s quality management policies or procedures may provide that a peer review conducted under standards established by the AICPA may be a substitute for the inspection of engagement documentation, reports, and clients’ financial statements for some or all engagements for the period covered by the peer review.</u></p>	<p>Specific to ASB jurisdiction</p>
<p>A168. <u>A peer review may result in findings or deficiencies. However, the definitions of findings and deficiencies in this SQMS are different than the definitions of those terms in AICPA Standards for Performing and Reporting on Peer Reviews.³ Accordingly, findings and deficiencies may be evaluated differently for peer review purposes than for purposes of this SQMS. Findings or deficiencies identified in a firm’s system of quality management may not necessarily result in a peer review finding or deficiency; similarly, peer review findings or deficiencies may not necessarily equate to findings or deficiencies in a firm’s system of quality management. As with other items identified in the firm’s monitoring activities, the firm would need to assess any peer review findings or deficiencies to determine the impact on the firm’s evaluation of its system of quality management.</u></p>	<p>Specific to ASB jurisdiction</p>
<p><u>Individuals Performing the Monitoring Activities</u> (Ref: par. 39(b) 40)</p>	
<p>A169. <u>It is important that individuals performing the monitoring activities have the competence, capabilities, time, and objectivity to perform the monitoring activities. Each of these attributes is equally essential. In some circumstances, there may not be personnel who have the competence, capabilities, time, and objectivity to perform the monitoring activities. In these circumstances, the firm may use network services or a service provider to perform the monitoring activities.</u></p>	<p>Par. A169-A174 re-ordered and expanded to address self-review threat in more depth</p>

³ Paragraphs 70 and 110, PRP section 1000, [AICPA Standards for Performing and Reporting on Peer Reviews \(AICPA, Professional Standards\)](#).

<p>A170.A155 The provisions of relevant ethical requirements are relevant in designing the policies or procedures addressing the objectivity of the individuals performing the monitoring activities. A self-review threat may arise when an individual who performs: □ an inspection of an engagement was:</p>	
<p>○ In the case of an audit of financial statements, an engagement team member or the engagement quality reviewer of that engagement or an engagement for a subsequent financial period; or</p>	
<p>○ For all other engagements, an engagement team member or the engagement quality reviewer of that engagement. <u>A self-review threat may also arise when an individual involved in operating the response to a quality risk is performing the monitoring of that response. For example, a self-review threat may arise if an engagement partner who is responsible for accepting their own client engagements is also responsible for monitoring compliance with the firm’s client acceptance policies and procedures.</u></p>	
<p>□ Another type of monitoring activity had participated in designing, executing or operating the response being monitored.</p>	
<p>A156. In some circumstances, for example, in the case of a less complex firm, there may not be personnel who have the competence, capabilities, time or objectivity to perform the monitoring activities. In these circumstances, the firm may use network services or a service provider to perform the monitoring activities.</p>	
<p>A171. <u>This SQMS does not preclude an individual from performing monitoring activities, including inspections, of their own compliance with a quality management system. However, such self-inspections may be less effective than compliance inspections by another qualified individual. When an individual inspects their own compliance with the firm’s policies and procedures, the firm has a higher risk that noncompliance with policies and procedures will not be detected or reported. To effectively monitor one’s own compliance, it is necessary that an individual be able to critically review their own performance, assess their own strengths and weaknesses, and maintain an attitude of continual improvement.</u></p>	
<p>A172. <u>Responses that may provide safeguards against the self-review threat and lessen the likelihood of deficiencies in the system of quality management include the following actions:</u></p>	

<ul style="list-style-type: none"> • <u>Fostering a commitment to continuing professional education and providing effective training programs so that personnel stay current on accounting, auditing, and quality management standards</u> 	
<ul style="list-style-type: none"> • <u>Providing training on how to perform monitoring inspections and requiring the use of peer review or other inspection checklists</u> 	
<ul style="list-style-type: none"> • <u>Requiring the passage of time after the completion of an engagement before self-inspections are performed</u> 	
<p>A173. <u>The firm may have responses in place to address quality risks other than the self-review threat that may be particularly helpful when self-inspections are performed, such as the following actions:</u></p>	
<ul style="list-style-type: none"> • <u>Establishing strong client acceptance and engagement continuance policies that address the risk of the firm accepting or continuing engagements it doesn't have the competency and resources to perform</u> 	
<ul style="list-style-type: none"> • <u>Establishing consultation policies that require engagement teams to consult when they encounter technical accounting and auditing difficulties</u> 	
<ul style="list-style-type: none"> • <u>Taking corrective action in response to the results identified by the firm's internal monitoring, engagement quality reviews, peer review results or other external inspections; for example, inspections by the U.S. Department of Labor</u> 	
<ul style="list-style-type: none"> • <u>Requiring the use of an external service provider to perform engagement quality reviews or monitoring activities when</u> 	
<ul style="list-style-type: none"> <ul style="list-style-type: none"> ○ <u>deficiencies identified by the firm's monitoring activities, peer reviewers or other external inspections indicate that self-inspection is not effective, or</u> 	

<p><u>o</u> changes in conditions and the environment within the firm (such as obtaining clients in an industry not previously serviced or significantly changing the size of the firm) occur.</p>	
<p><i>Evaluating Findings and Identifying Deficiencies (Ref: par. 16(a), 40-17 and 41-42)</i></p>	
<p>A174.A157.—The firm accumulates findings from the performance of monitoring activities, external inspections, and other relevant sources.</p>	
<p>A158. Information accumulated by the firm from the monitoring activities, external inspections, and other relevant sources may reveal other observations about the firm’s system of quality management, such as:</p>	
<ul style="list-style-type: none"> <u>•</u> • actions, behaviors, or conditions that have given rise to positive outcomes in the context of quality or the effectiveness of the system of quality management; or 	
<ul style="list-style-type: none"> <u>•</u> • similar circumstances wherein which no findings were noted (e.g. for example, engagements wherein which no findings were noted, and the engagements have a similar nature to the engagements wherein which findings were noted). 	
<p>Other observations may be useful to the firm asbecause they may assist the firm in investigating the root cause(s)causes of identified deficiencies, indicate practices that the firm can support or apply more extensively (e.g. for example, across all engagements), or highlight opportunities for the firm to enhance the system of quality management.</p>	
<p>A175. A159.The firm exercises professional judgment in determining whether findings, individually or in combination with other findings, give rise to a deficiency in the system of quality management. In making the judgment, the firm may need to take into account the relative importance of the findings in the context of the quality objectives, quality risks, responses, or other aspects of the system of quality management to which they relate. The firm’s judgments may be affected by quantitative and qualitative factors relevant to the findings. In some circumstances, the firm may determine it appropriate to obtain more information about the findings in order to determine whether a deficiency exists. Not all findings, including engagement findings, will be a deficiency.</p>	
<p>A176. A160.Examples of quantitative and qualitative factors that a firm may consider in determining whether findings give rise to a deficiency include the following:</p>	

<p><i>Quality risks and responses</i></p>	
<ul style="list-style-type: none"> • If the findings relate to a response, <u>factors such as the following</u>: 	
<ul style="list-style-type: none"> ○ How the response is designed; for example, the nature of the response, the frequency of its occurrence (if applicable), and the relative importance of the response to addressing the quality risk(s)<u>risks</u> and achieving the quality objective(s)<u>objectives</u> to which it relates. 	
<ul style="list-style-type: none"> ○ The nature of the quality risk to which the response relates, and the extent to which the findings indicate that the quality risk has not been addressed. 	
<ul style="list-style-type: none"> ○ Whether there are other responses that address the same quality risk and whether there are findings for those responses. 	
<p><i>Nature of the findings and their pervasiveness</i></p>	
<ul style="list-style-type: none"> • The nature of the findings; for example, findings related to leadership actions and behaviors may be qualitatively significant, given the pervasive effect this could have on the system of quality management as a whole. 	
<ul style="list-style-type: none"> • Whether the findings, in combination with other findings, indicate a trend or systemic issue; for example, similar engagement findings that appear on multiple engagements may indicate a systemic issue. 	
<p><i>Extent of Monitoring Activity and Extent of Findings</i></p>	
<ul style="list-style-type: none"> • The extent of the monitoring activity from which the findings arose, including the number or size of the selections. 	
<ul style="list-style-type: none"> • The extent of the findings in relation to the selection covered by the monitoring activity, and in relation to the expected deviation rate; for example, in the case of inspection of engagements, the number of engagements selected <u>wherein which</u> the findings were identified, relative to the total number of engagements selected, and the expected deviation rate set by the firm 	
<p>A177. A161. Evaluating findings and identifying deficiencies and evaluating the severity and pervasiveness of an identified deficiency, including investigating the root cause(s)<u>causes</u> of an identified deficiency, are part of an iterative and non-linear process. Examples of how the process of evaluating findings and identifying deficiencies,</p>	

<p>evaluating identified deficiencies, including investigating the root cause(s) of identified deficiencies, is iterative and non-linear<u>follow:</u></p>	
<ul style="list-style-type: none"> In investigating the root cause(s)<u>causes</u> of an identified deficiency, the firm may identify a circumstance that has similarities to other circumstances wherein which there were findings that were not considered a deficiency<u>deficiencies</u>. As a result, the firm adjusts its evaluation of the other findings and classifies them as a deficiency<u>deficiencies</u>. 	
<ul style="list-style-type: none"> In evaluating the severity and pervasiveness of an identified deficiency, the firm may identify a trend or systemic issue that correlates with other findings that are not considered deficiencies. As a result, the firm adjusts its evaluation of the other findings and also classifies them as deficiencies. 	
<p>A178. A162. The results of monitoring activities, results of external inspections, and other relevant information (e.g. for example, network monitoring activities or complaints and allegations) may reveal information about the effectiveness of the monitoring and remediation process. For example, the results of external inspections may provide information about the system of quality management that has not been identified by the firm’s monitoring and remediation process, which may highlight a deficiency in that process.</p>	
<p>Evaluating Identified Deficiencies (Ref: par. 41)</p>	
<p>A163. 42)</p>	
<p>A179. Factors the firm may consider in evaluating the severity and pervasiveness of an identified deficiency include <u>the following:</u></p>	
<ul style="list-style-type: none"> The nature of the identified deficiency, including the aspect of the firm’s system of quality management to which the deficiency relates, and whether the deficiency is in the design, implementation, or operation of the system of quality management; 	
<ul style="list-style-type: none"> In the case of identified deficiencies related to responses, whether there are compensating responses to address the quality risk to which the response relates; 	
<ul style="list-style-type: none"> The root cause(s)<u>causes</u> of the identified deficiency; 	
<ul style="list-style-type: none"> The frequency with which the matter giving rise to the identified deficiency occurred;and 	

<ul style="list-style-type: none"> The magnitude of the identified deficiency, how quickly it occurred, and the duration of time that it existed and had an effect on the system of quality management. 	
<p>A180. A164.—The severity and pervasiveness of identified deficiencies affects the evaluation of the system of quality management that is undertaken by the individual(s) <u>or individuals</u> assigned ultimate responsibility and accountability for the system of quality management.</p>	
<p><i>Root Cause of the Identified Deficiencies (Ref: par-41(a). <u>42a</u>)</i></p>	
<p>A181. A165The objective of investigating the root cause(s)<u>causes</u> of identified deficiencies is to understand the underlying circumstances that caused the deficiencies to enable the firm to:</p>	
<ul style="list-style-type: none"> evaluate the severity and pervasiveness of the identified deficiency; and 	
<ul style="list-style-type: none"> appropriately remediate the identified deficiency. 	
<p>Performing a root cause analysis involves those performing the assessment exercising<u>exercise of</u> professional judgment based on the evidence available by those performing the assessment.</p>	
<p>A182. A166The nature, timing, and extent of the procedures undertaken to understand the root cause(s)<u>causes</u> of an identified deficiency may also be affected by the nature and circumstances of the firm, such as <u>the following</u>:</p>	
<ul style="list-style-type: none"> The complexity and operating characteristics of the firm. 	
<ul style="list-style-type: none"> The size of the firm. 	
<ul style="list-style-type: none"> The geographical dispersion of the firm. 	
<ul style="list-style-type: none"> How the firm is structured or the extent to which the firm concentrates or centralizes its processes or activities. For example, in the case of a less complex firm with a single location, the firm’s procedures to understand the root causes of a deficiency may be simple because the information to inform the understanding may be readily available and concentrated, and the root causes may be more apparent. In the case of a more complex firm with multiple locations, the procedures to understand the root causes of a deficiency may include using individuals specifically trained on investigating the root causes 	

<p>of identified deficiencies and developing a methodology with more formalized procedures for identifying root causes.</p>	
<ul style="list-style-type: none"> The possible severity of the identified deficiency; for example, the firm’s procedures to understand the root causes of an identified deficiency may be more rigorous in circumstances in which the deficiency has been identified across multiple engagements, or there is an indication that policies or procedures have high rates of noncompliance. 	
<p>A183. A167. In investigating the root cause(s)<u>causes</u> of identified deficiencies, the firm may consider why deficiencies did not arise in other circumstances that are of a similar nature to the matter to which the identified deficiency relates. Such information may also be useful in determining how to remediate an identified deficiency. For example of when a deficiency did not arise in other circumstances of a similar nature, and how this information assists the firm in investigating the root cause(s) of identified deficiencies. <u>For</u> the firm may determine that a deficiency exists because similar findings have occurred across multiple engagements. However, the findings have not occurred in several other engagements within the same population being tested. By contrasting the engagements, the firm concludes that the root cause of the identified deficiency is a lack of appropriate involvement by the engagement partners at key stages of the engagements.</p>	
<p>A184. A168. Identifying a root cause(s)<u>causes</u> that is<u>are</u> appropriately specific may support the firm’s process for remediating identified deficiencies. For example of identifying a root cause(s) that is appropriately specific. <u>For</u> the firm may identify that engagement teams performing audits of financial statements are failing to obtain sufficient appropriate audit evidence on accounting estimates where<u>when</u> management’s assumptions have a high degree of subjectivity. While<u>Although</u> the firm notes that these engagement teams are not exercising<u>maintaining</u> appropriate professional skepticism, the underlying root cause of this issue may relate to another matter, such as a cultural environment that does not encourage engagement team members to question individuals with greater authority or insufficient direction, supervision, and review of the work performed on the engagements.</p>	
<p>A185. A169. In addition to investigating the root cause(s)<u>causes</u> of identified deficiencies, the firm may also investigate the root cause(s)<u>causes</u> of positive outcomes as<u>because</u> doing so may reveal</p>	

<p>opportunities for the firm to improve, or further enhance, the system of quality management.</p>	
<p><i>Responding to Identified Deficiencies (Ref: par. 4243)</i></p>	
<p>A186. A170 The nature, timing, and extent of remedial actions may depend on a variety of other factors, including <u>the following</u>:⁻</p>	
<ul style="list-style-type: none"> • The root cause(s)-<u>causes</u> 	
<ul style="list-style-type: none"> • The severity and pervasiveness of the identified deficiency and, therefore, the urgency with which it needs to be addressed. 	
<ul style="list-style-type: none"> • The effectiveness of the remedial actions in addressing the root cause(s)<u>causes</u>, such as whether the firm needs to implement more than one remedial action in order to effectively address the root cause(s)<u>causes</u>, or needs to implement remedial actions as interim measures until the firm is able to implement more effective remedial actions. 	
<p>A187. A171 In some circumstances, the remedial action may include establishing additional quality objectives, or quality risks or responses may be added or modified, because it is determined that they are not appropriate.</p>	
<p>A188. A172 In circumstances when<u>in which</u> the firm determines that the root cause of an identified deficiency relates to a resource provided by a service provider, the firm may also:</p>	
<ul style="list-style-type: none"> • consider whether to continue using the resource provided by the service provider.⁻<u>or</u> 	
<ul style="list-style-type: none"> • communicate the matter to the service provider. 	
<p>The firm is responsible for addressing the effect of the identified deficiency related to a resource provided by a service provider on the system of quality management and taking action to prevent the deficiency from recurring with respect to the firm’s system of quality management. However, the firm is not ordinarily responsible for remediating the identified deficiency on behalf of the service provider or further investigating the root cause of the identified deficiency at the service provider.</p>	
<p><i>Findings About a Particular Engagement (Ref: par. 4546)</i></p>	
<p>A189. A173 <u>AU-C section 585, Consideration of Omitted Procedures After the Report Release Date, addresses the auditor’s responsibilities</u> in circumstances when<u>in which</u> procedures were omitted, or the report issued is inappropriate. <u>In such circumstances relating to other assurance</u></p>	<p>To clarify</p>

<p><u>and attest engagements</u>, the action taken by the firm may include <u>the following</u>:</p>	
<ul style="list-style-type: none"> • Consulting with appropriate individuals regarding the appropriate action. 	
<ul style="list-style-type: none"> • Discussing the matter with management of the entity or those charged with governance. 	
<ul style="list-style-type: none"> • Performing the omitted procedures. 	
<p>The actions taken by the firm do not relieve the firm of the responsibility to take further actions relating to the finding in the context of the system of quality management, including evaluating the findings to identify deficiencies and, when a deficiency exists, investigating the root cause(s)<u>causes</u> of the identified deficiency.</p>	
<p><i>Ongoing Communication Related to the Monitoring and Remediation</i> (Ref: par. 46<u>47</u>)</p>	
<p>A190. A174The information communicated about the monitoring and remediation to the individual(s) <u>or individuals</u> assigned ultimate responsibility and accountability for the system of quality management may be communicated on an ongoing basis or periodically. The individual(s) <u>or individuals</u> may use the information in multiple ways, for example. <u>Examples follow</u>:</p>	
<ul style="list-style-type: none"> • As a basis for further communications to personnel about the importance of quality. 	
<ul style="list-style-type: none"> • To hold individuals accountable for their roles assigned to them. 	
<ul style="list-style-type: none"> • To identify key concerns about the system of quality management in a timely manner. 	
<p>The information also provides a basis for the evaluation of the system of quality management, and conclusion thereon, as required by paragraphs 53–54<u>56</u>.</p>	
<p>Network Requirements or Network Services (Ref: par. 48<u>49</u>)</p>	
<p>A191. A175In some circumstances, the firm may belong to a network. Networks may establish requirements regarding the firm’s system of quality management or may make services or resources available that the firm may choose to implement or use in the design, implementation, and operation of its system of quality management. Such requirements or services may be intended to promote the consistent performance of</p>	

<p>quality engagements across the firms that belong to the network. The extent to which the network will provide the firm with quality objectives, quality risks, and responses that are common across the network will depend on the firm’s arrangements with the network.</p>	
<p>A192. Examples of network requirements <u>include the following:</u></p>	
<ul style="list-style-type: none"> • Requirements for the firm to include additional quality objectives or quality risks in the firm’s system of quality management that are common across the network firms. 	
<ul style="list-style-type: none"> • Requirements for the firm to include responses in the firm’s system of quality management that are common across the network firms. Such responses designed by the network may include network policies or procedures that specify the leadership roles and responsibilities, including how the firm is expected to assign authority and responsibility within the firm, or resources, such as network -developed methodologies for the performance of<u>performing</u> engagements or IT applications. 	
<ul style="list-style-type: none"> • Requirements that the firm be subject to the network’s monitoring activities. These monitoring activities may relate to network requirements (e.g. for example, monitoring that the firm has implemented the network’s methodology appropriately), or to the firm’s system of quality management in general. 	
<p>A193. Examples of network services • <u>include</u> services or resources that are optional for the firm to use in its system of quality management or in the performance of<u>performing</u> engagements, such as voluntary training programs, use of component auditors or experts<u>specialists</u> from within the network, or use of a service delivery center established at the network level, or by another network firm or group of network firms.</p>	
<p>A194. A176. The network may establish responsibilities for the firm in implementing the network requirements or network services. Examples of responsibilities for the firm in implementing network requirements or network services <u>follow:</u></p>	
<ul style="list-style-type: none"> • The firm is required to have certain IT infrastructure and IT processes in place to support an IT application provided by the network that the firm uses in the system of quality management. 	

<ul style="list-style-type: none"> The firm is required to provide firm-wide training on the methodology provided by the network, including when updates are made to the methodology. 	
<p>A195. A177. The firm’s understanding of the network requirements or network services and the firm’s responsibilities relating to the implementation thereof may be obtained through inquiries of, or documentation provided by, the network about matters such as <u>the following</u>:</p>	
<ul style="list-style-type: none"> The network’s governance and leadership. 	
<ul style="list-style-type: none"> The procedures undertaken by the network in designing, implementing, and, if applicable, operating, the network requirements or network services. 	
<ul style="list-style-type: none"> How the network identifies and responds to changes that affect the network requirements or network services or other information, such as changes in the professional standards or information that indicates a deficiency in the network requirements or network services. 	
<ul style="list-style-type: none"> How the network monitors the appropriateness of the network requirements or network services, which may include through the network firms’ monitoring activities, and the network’s processes for remediating identified deficiencies. 	
<p><i>Network Requirements or Network Services in the Firm’s System of Quality Management (Ref: par. 4950)</i></p>	
<p>A196. A178 The characteristics of the network requirements or network services are a condition, event, circumstance, action, or inaction in identifying and assessing quality risks. <u>An</u> example of a network requirement or network service that gives rise to a quality risk <u>is as follows</u>.</p>	
<p>The network may require the firm to use an IT application for the acceptance and continuance of client relationships and specific engagements that is standardized across the network. This may give rise to a quality risk that the IT application does not address matters in local law or regulation that need to be considered by the firm in accepting and continuing client relationships and specific engagements.</p>	
<p>A197. A179. The purpose of the network requirements may include the promotion of consistent performance of quality engagements across the network firms. The firm may be expected by the network to implement</p>	

<p>the network requirements; however, the firm may need to adapt or supplement the network requirements such that they are appropriate for the nature and circumstances of the firm and its engagements.</p>	
<p>A198. <u>Examples of how the network requirements or network services may need to be adapted or supplemented include the following:</u></p>	

<p><i>Examples of how the network requirements or networks services may need to be adapted or supplemented</i></p>	
<p><i>Network requirement or network service</i></p>	<p><i>How the firm adapts or supplements the network requirement or network service</i></p>
<p>The network requires the firm to include certain quality risks in the system of quality management, so that all firms in the network address the quality risks. <u>The network does not provide an assessment of the quality risks.</u></p>	<p>As part of identifying and assessing quality risks, the firm includes <u>assesses</u> the quality risks that are required by the network.</p> <p>The firm also designs and implements responses to address the <u>assessed</u> quality risks that are required by the network.</p>
<p>The network requires that the firm design and implement certain responses.</p>	<p>As part of designing and implementing responses, the firm determines:</p> <ul style="list-style-type: none"> • which <u>assessed</u> quality risks the responses address. • how the responses required by the network will be incorporated into the firm’s system of quality management, given the nature and circumstances of the firm. This may include tailoring the response to reflect the nature and circumstances of the firm and its <u>the</u> engagements (e.g. performed by the firm <u>(for example,</u> tailoring a methodology to include matters related to law or

	regulation).
<p>The firm uses individuals from other network firms as component auditors.</p> <p>Network requirements are in place that drive a high degree of commonality across the network firms’ systems of quality management. The network requirements include specific criteria that apply to individuals assigned to work on a component for a group audit.</p>	<p>The firm establishes policies or procedures that require the engagement team to confirm with the component auditor (i.e. that is, the other network firm) that the individuals assigned to the component meet the specific criteria set out in the network requirements.</p>

<p>A199. A180. In some circumstances, in adapting or supplementing the network requirements or network services, the firm may identify possible improvements to the network requirements or network services and may communicate these improvements to the network.</p>	
<p><i>Monitoring Activities Undertaken by the Network on the Firm’s System of Quality Management (Ref: par. 5051c)</i></p>	
<p>A200. A181. The results of the network’s monitoring activities of the firm’s system of quality management may include information such as <u>the following</u>:</p>	
<ul style="list-style-type: none"> • A description of the monitoring activities, including their nature, timing, and extent; 	
<ul style="list-style-type: none"> • Findings, identified deficiencies, and other observations about the firm’s system of quality management (e.g. for example, positive outcomes or opportunities for the firm to improve, or further enhance, the system of quality management); and 	
<ul style="list-style-type: none"> • The network’s evaluation of the root cause(s) <u>causes</u> of the identified deficiencies, the assessed effect of the identified deficiencies, and recommended remedial actions; 	
<p><i>Monitoring Activities Undertaken by the Network Across the Network Firms (Ref: par. 5452b)</i></p>	

<p>A201. A182—The information from the network about the overall results of the network’s monitoring activities undertaken across the network firms’ systems of quality management may be an aggregation or summary of the information described in paragraph A184<u>193</u>, including trends and common areas of identified deficiencies across the network, or positive outcomes that may be replicated across the network. Such information may:</p>	
<ul style="list-style-type: none"> • be used by the firm: 	
<ul style="list-style-type: none"> <ul style="list-style-type: none"> ○ in identifying and assessing quality risks, <u>and</u> 	
<ul style="list-style-type: none"> <ul style="list-style-type: none"> ○ as part of other relevant information considered by the firm in determining whether deficiencies exist in the network requirements or network services used by the firm in its system of quality management. 	
<ul style="list-style-type: none"> • be communicated to group engagement partners, in the context of considering the competence and capabilities of component auditors from a network firm who are subject to common network requirements (e.g. for example, common quality objectives, quality risks, and responses). 	
<p>A202.A183.In some circumstances, the firm may obtain information from the network about deficiencies identified in a network firm’s system of quality management that affects the firm. The network may also gather information from network firms regarding the results of external inspections over network firms’ systems of quality management. In some instances, law or regulation in a particular jurisdiction may prevent the network from sharing information with other network firms or may restrict the specificity of such information.</p>	
<p>A203. A184.In circumstances when<u>in which</u> the network does not provide the information about the overall results of the network’s monitoring activities across the network firms, the firm may take further actions, such as:</p>	
<ul style="list-style-type: none"> • discussing the matter with the network, <u>and</u> 	
<ul style="list-style-type: none"> • determining the effect on the firm’s engagements, <u>and</u> communicating the effect to engagement teams. 	

<p>Deficiencies in Network Requirements or Network Services Identified by the Firm (Ref: par. 52<u>53</u>)</p>	
<p>A204. A185As network requirements or network services used by the firm form part of the firm’s system of quality management, they are also subject to the requirements of this ISQM<u>SQMS</u> regarding monitoring and remediation. The network requirements or network services may be monitored by the network, the firm, or a combination of both; <u>for</u> example of when a network requirement or network service is monitored by both the network and the firm, a network may undertake monitoring activities at a network level for a common methodology. The firm <u>may</u> also monitors<u>monitor</u> the application of the methodology by engagement team members through performing engagement inspections.</p>	
<p>A205. A186–In designing and implementing the remedial actions to address the effect of the identified deficiency in the network requirements or network services, the firm may:</p>	
<ul style="list-style-type: none"> • understand the planned remedial actions by the network, including whether the firm has any responsibilities for implementing the remedial actions; and 	
<ul style="list-style-type: none"> • consider whether supplementary remedial actions need to be taken by the firm to address the identified deficiency and the related root cause(s)<u>causes</u>, such as when: 	
<ul style="list-style-type: none"> ○ the network has not taken appropriate remedial actions; or 	
<ul style="list-style-type: none"> ○ the network’s remedial actions will take time to effectively address the identified deficiency. 	
<p>Evaluating the System of Quality Management (Ref: par. 53<u>54</u>)</p>	
<p>A206. A187The individual(s) <u>or individuals</u> assigned ultimate responsibility and accountability for the system of quality management may be assisted by other individuals in performing the evaluation. Nevertheless, the individual(s) <u>or individuals</u> assigned ultimate responsibility and accountability for the system of quality management remains<u>remain</u> responsible and accountable for the evaluation.</p>	
<p>A207. A188–The point in time at which the evaluation is undertaken may depend on the circumstances of the firm; and may coincide with the fiscal year <u>end</u> of the firm or the completion of an annual monitoring cycle.</p>	

<p>A208. A189–The information that provides the basis for the evaluation of the system of quality management includes the information communicated to the individual(s)<u>individuals</u> assigned ultimate responsibility and accountability for the system of quality management in accordance with paragraph 46<u>47</u>.</p>	
<p>A209.<u>An example of</u> scalability examples–to demonstrate how the information that provides the basis for the evaluation of the system of quality management may be obtained <u>in firms of different complexity is as follows:</u></p>	
<ul style="list-style-type: none"> • In a less complex firm, the individual(s) <u>or individuals</u> assigned ultimate responsibility and accountability for the system of quality management may be directly involved in the monitoring and remediation and will, therefore, <u>will</u> be aware of the information that supports the evaluation of the system of quality management. 	
<ul style="list-style-type: none"> • In a more complex firm, the individual(s) <u>or individuals</u> assigned ultimate responsibility and accountability for the system of quality management may need to establish processes to collate, summarize, and communicate the information needed to evaluate the system of quality management. 	
<p><i>Concluding on the System of Quality Management (Ref: par. 54<u>55</u>)</i></p>	
<p>A210. A190In the context of this ISQMS<u>SQMS</u>, it is intended that the operation of the system as a whole provides the firm with reasonable assurance that the objectives of the system of quality management are being achieved. In concluding on the system of quality management, the individual(s) <u>or individuals</u> assigned ultimate responsibility and accountability for the system of quality management may, in using the results of the monitoring and remediation process, consider the following:</p>	
<ul style="list-style-type: none"> • The severity and pervasiveness of identified deficiencies, and the effect on the achievement of the objectives of the system of quality management; 	
<ul style="list-style-type: none"> • Whether remedial actions have been designed and implemented by the firm, and whether the remedial actions taken up to the time of the evaluation are effective; and 	

<ul style="list-style-type: none"> Whether the effect of identified deficiencies on the system of quality management have been appropriately corrected, such as whether further actions have been taken in accordance with paragraph 45-46. 	
<p>A211. A191.—There may be circumstances when<u>in which</u> identified deficiencies that are severe (including identified deficiencies that are severe and pervasive) have been appropriately remediated and the effect of them corrected at the point in time of the evaluation. In such cases, the individual(s) <u>or individuals</u> assigned ultimate responsibility and accountability for the system of quality management may conclude that the system of quality management provides the firm with reasonable assurance that the objectives of the system of quality management are being achieved.</p>	
<p>A212. A192.—An identified deficiency may have a pervasive effect on the design, implementation, and operation of the system of quality management when, for example, <u>the following apply</u>:</p>	
<ul style="list-style-type: none"> The deficiency affects several components or aspects of the system of quality management. 	
<ul style="list-style-type: none"> The deficiency is confined to a specific component or aspect of the system of quality management, but is fundamental to the system of quality management. 	
<ul style="list-style-type: none"> The deficiency affects several business units or geographical locations of the firm. 	
<ul style="list-style-type: none"> The deficiency is confined to a business unit or geographical location, but the business unit or location affected is fundamental to the firm overall. 	
<ul style="list-style-type: none"> The deficiency affects a substantial portion of engagements that are of a certain type or nature. 	
<p>A213. <u>An</u> example of an identified deficiency that may be considered severe but not pervasive <u>is as follows</u>:</p>	
<p>The firm identifies a deficiency in <u>aone of its</u> smaller regional office of the firm<u>offices</u>. The identified deficiency relates to non-compliance with many firm policies or procedures. The firm determines that the culture in the regional office, particularly the actions and behavior of leadership in the regional office, which were overly focused on financial priorities, has</p>	

<p>contributed to the root cause of the identified deficiency. The firm determines that the effect of the identified deficiency is <u>as follows</u>:</p>	
<ul style="list-style-type: none"> • Severe, because it relates to the culture of the regional office and overall compliance with firm policies or procedures;and 	
<ul style="list-style-type: none"> • Not pervasive, because it is limited to the smaller regional office. 	
<p>A214. A193.—The individual(s) <u>or individuals</u> assigned ultimate responsibility and accountability for the system of quality management may conclude that the system of quality management does not provide the firm with reasonable assurance that the objectives of the system of quality management are being achieved in circumstances when<u>in which</u> identified deficiencies are severe and pervasive, actions taken to remediate the identified deficiencies are not appropriate, and the effect of the identified deficiencies have not been appropriately corrected.</p>	
<p>A215. <u>An</u> example of an identified deficiency that may be considered severe and pervasive <u>is as follows</u>:</p>	
<p>The firm identifies a deficiency in a regional office, which is the <u>firm's</u> largest office of the firm and provides financial, operational, and technical support for the entire region. The identified deficiency relates to non-compliance with many firm policies or procedures. The firm determines that the culture in the regional office, particularly the actions and behavior of leadership in the regional office, which were overly focused on financial priorities, has contributed to the root cause of the identified deficiency. The firm determines that the effect of the identified deficiency is <u>as follows</u>:</p>	
<ul style="list-style-type: none"> • Severe, because it relates to the culture of the regional office and overall compliance with firm policies or procedures;and 	
<ul style="list-style-type: none"> • Pervasive, because the regional office is the largest office and provides support to many other offices, and the non-compliance with firm policies or procedures may have had a broader effect on the other offices. 	
<p>A216. A194.—It may take time for the firm to remediate identified deficiencies that are severe and pervasive. As the firm continues to take action to remediate the identified deficiencies, the pervasiveness of the identified deficiencies may be diminished, and it may be determined that the identified deficiencies are still severe, but no longer severe and pervasive. In such cases, the individual(s) <u>or individuals</u> assigned</p>	

<p>ultimate responsibility and accountability for the system of quality management may conclude that, except for matters related to identified deficiencies that have a severe but not pervasive effect on the design, implementation, and operation of the system of quality management, the system of quality management provides the firm with reasonable assurance that the objectives of the system of quality management are being achieved.</p>	
<p>A217. A195. This ISQM<u>SQMS</u> does not require the firm to obtain an independent assurance<u>evaluation (for example, a peer review or SOC report)</u> on its system of quality management, annually or preclude the firm from doing so.</p>	
<p><i>Taking Prompt and Appropriate Action and Further Communication (Ref: par. 55<u>56</u>)</i></p>	
<p>A218. A196. In circumstances when<u>in which</u> the individual(s) <u>or individuals</u> assigned ultimate responsibility and accountability for the system of quality management reaches<u>reach</u> the conclusion described in paragraph 54(b) or 54(c), the prompt and appropriate action taken by the firm may include <u>the following</u>:</p>	
<ul style="list-style-type: none"> • Taking measures to support the performance of<u>performing</u> engagements through assigning more resources or developing more guidance and to confirm that reports issued by the firm are appropriate in the circumstances, until such time as the identified deficiencies are remediated, and communicating such measures to engagement teams. 	
<ul style="list-style-type: none"> • Obtaining legal advice. 	
<p>A219.A197. In some circumstances, the firm may have an independent governing body that has non-executive oversight of the firm. In such circumstances, communications may include informing the independent governing body.</p>	
<p></p>	
<p>A220. A198. Examples of circumstances when<u>in which</u> it may be appropriate for the firm to communicate to external parties about the evaluation of the system of quality management <u>include the following</u>:</p>	
<ul style="list-style-type: none"> • When the firm belongs to a network. 	
<ul style="list-style-type: none"> • When other network firms use the work performed by the firm, for example, in the case of a group audit. 	

<ul style="list-style-type: none"> When a report issued by the firm is determined by the firm to be inappropriate as a result of the failure of the system of quality management, and management or those charged with governance of the entity need to be informed. 	
<ul style="list-style-type: none"> When law or regulation requires the firm to communicate to an oversight authority or a regulatory body. 	
<p>Performance Evaluations (Ref: par. 5657)</p>	
<p>A221. A199 Periodic performance evaluations promote accountability. In considering the performance of an individual, the firm may take <u>the following</u> into account:</p>	
<ul style="list-style-type: none"> The results of the firm’s monitoring activities for aspects of the system of quality management that relate to the responsibility of the individual. In some circumstances, the firm may set targets for the individual and measure the results of the firm’s monitoring activities against those targets. 	
<ul style="list-style-type: none"> The actions taken by the individual in response to identified deficiencies that relate to the responsibility of that individual, including the timeliness and effectiveness of such actions. 	
<p>A222. <u>An example of scalability</u> examples to demonstrate how the firm <u>firms of different complexity</u> may undertake the performance evaluations <u>is as follows</u>:</p>	
<ul style="list-style-type: none"> In a less complex firm, the firm may engage a service provider to perform the evaluation, or the results of the firm’s monitoring activities may provide an indication of the performance of the individual. 	
<ul style="list-style-type: none"> In a more complex firm, the performance evaluations may be undertaken by an independent non-executive member of the firm’s governing body, or a special committee overseen by the firm’s governing body. 	
<p>A223.A200—A positive performance evaluation may be rewarded through compensation, promotion, and other incentives that focus on the individual’s commitment to quality, and reinforce accountability. On the other hand, the firm may take corrective actions to address a negative performance evaluation that may affect the firm’s achievement of its quality objectives.</p>	

<p>Public Sector Considerations</p> <p>A201. In the case of the public sector, it may not be practicable to perform a performance evaluation of the individual(s) assigned ultimate responsibility and accountability for the system of quality management, or to take actions to address the results of the performance evaluation, given the nature of the individual's appointment. Nevertheless, performance evaluations may still be undertaken for other individuals in the firm who are assigned operational responsibility for aspects of the system of quality management.</p>	<p>Not relevant in ASB jurisdiction</p>
<p>Documentation (Ref: par. 5758–5960)</p>	
<p>A224. A202. Documentation provides evidence that the firm complies with this ISQMS<u>SQMS</u>, as well as law, regulation, or relevant ethical requirements. It may also be useful for training personnel and engagement teams, ensuring the retention of organizational knowledge, and providing a history of the basis for decisions made by the firm about its system of quality management. It is neither necessary nor practicable for the firm to document every matter considered, or judgment made, about its system of quality management. Furthermore, compliance with this ISQMS<u>SQMS</u> may be evidenced by the firm through its information and communication component, documents or other written materials, or IT applications that are integral to the components of the system of quality management.</p>	
<p>A225. A203. Documentation may take the form of<u>be</u> formal (<u>for example,</u> written manuals, checklists, and forms), may be informally documented (e.g., e-mail)<u>informal (for example, email</u> communication or postings on websites), or may be held in IT applications or other digital forms (<u>e.g. for example,</u> in databases). Factors that may affect the firm’s judgments about the form, content, and extent of documentation, including how often documentation is updated, may include <u>the following</u>:</p>	
<ul style="list-style-type: none"> • The complexity of the firm and the number of offices; 	
<ul style="list-style-type: none"> • The nature and complexity of the firm’s practice and organization; 	
<ul style="list-style-type: none"> • The nature of engagements the firm performs and the nature of the entities for whom engagements are performed; 	
<ul style="list-style-type: none"> • The nature and complexity of the matter being documented, such as whether it relates to an aspect of the system of quality management that has changed or an area of greater quality risk, and the complexity of the judgments relating to the matter; 	

<ul style="list-style-type: none"> • The frequency and extent of changes in the system of quality management. 	
<p>In a less complex firm, it may not be necessary to have documentation supporting matters communicated because informal communication methods may be effective. Nevertheless, a less complex firm may determine it appropriate to document such communications in order to provide evidence that they occurred.</p>	
<p>A226. A204. In some instances, an external oversight authority may establish documentation requirements, either formally or informally, for example, as a result of the outcome of external inspection findings. Relevant ethical requirements may also include specific requirements addressing documentation; for example, the IESBA AICPA code requires documentation of particular matters, including certain situations related to conflicts of interest, non-compliance with laws and regulations, and independence.</p>	
<p>A227. A205. The firm is not required to document the consideration of every condition, event, circumstance, action, or inaction for each quality objective, or each risk that may give rise to a quality risk. However, in documenting the quality risks and how the firm’s responses address the quality risks, the firm may document the reasons for the assessment given to the quality risks (i.e. <u>that is</u>, the considered occurrence and effect on the achievement of one or more quality objectives), in order to support the consistent implementation and operation of the responses.</p>	
<p>A228. A206. The documentation may be provided by the network, other network firms, or other structures or organizations within the network.</p>	

Document comparison by Workshare Compare on Tuesday, April 19, 2022
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Document 1 ID	IAASB-Quality-Management-ISQM-1-Quality-Management-for-Firms (for comparison).docx
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Document 2 ID	2A QM1 marked from January ASB meeting.docx
Description	2A QM1 marked from January ASB meeting.docx
Rendering set	Standard

Legend:	
Insertion	
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Format change	
Moved deletion	
Inserted cell	
Deleted cell	
Moved cell	
Split/Merged cell	
Padding cell	

Statistics:	
	Count
Insertions	2217
Deletions	2329
Moved from	30
Moved to	30
Style change	0
Format changed	0
Total changes	4606



~~INTERNATIONAL STANDARD~~ STATEMENT ON QUALITY MANAGEMENT
~~2~~ STANDARDS
ENGAGEMENT QUALITY REVIEWS

CONTENTS

	Paragraph
Introduction	
Scope of this ISQMS <u>SQMS</u>	1-4
The Firm’s System of Quality Management and Role of Engagement Teams	5–9
Authority of this ISQMS <u>SQMS</u>	10
Effective Date	11
Objective	12
Definitions	13
Requirements	
Applying, and Complying With, Relevant Requirements	14–16
Appointment and Eligibility of Engagement Quality Reviewers	17–23
Performance of the Engagement Quality Review	24–27
Documentation	28–30
Application and Other Explanatory Material	
Appointment and Eligibility of Engagement Quality Reviewers	A1– A24 <u>A27</u>
Performance of the Engagement Quality Review	A25 <u>A28</u> –A49
Documentation	A50-A53

Introduction

	Explanation of differences
Scope of This <u>Statement on Quality Management Standard</u> ISQM	
1. This International Standard <u>Statement</u> on Quality Management <u>Standards</u> (ISQM <u>SQMS</u>) deals with <u>addresses the following</u> :	AICPA Style
a. The appointment and eligibility of the engagement quality reviewer; and	AICPA Style
b. The engagement quality reviewer’s responsibilities relating to the performance and documentation of an engagement quality review.	
2. This ISQM <u>SQMS</u> applies to all engagements for which an engagement quality review is required to be performed in accordance with ISQM <u>4</u> <u>SQMS No. 1, A Firm’s System of Quality Management, including when the firm has determined that an engagement quality review is an appropriate response to assessed quality risks.</u> ¹ This ISQM is premised on the basis that the firm is subject to ISQM 1 or to national requirements that are at least as demanding. This ISQM <u>SQMS</u> is to be read in conjunction with <u>the AICPA Code of Professional Conduct (AICPA code) and other relevant ethical requirements.</u>	Specific to U.S.
3. An engagement quality review performed in accordance with this ISQM <u>SQMS</u> is a specified response that is designed and implemented by the firm in accordance with ISQM 1, SQMS No. 1. ² The performance of an engagement quality review is undertaken at the engagement level by the engagement quality reviewer on behalf of the firm.	
Scalability	
4. The nature, timing, and extent of the engagement quality reviewer’s procedures required by this ISQM <u>SQMS</u> vary depending on the nature and circumstances of the engagement or the entity. For example, the engagement quality reviewer’s procedures would likely be less extensive for engagements involving fewer significant judgments made by the engagement team, <u>the engagement quality reviewer’s procedures would likely be less extensive.</u>	To clarify; no change in meaning intended

¹ ~~International Standard Paragraph 35f of Statement~~ Paragraph 35f of Statement on Quality Management (~~ISQM~~ Standards (SQMS) 4) (previously International Standard Statement on Quality Control Standards) No. 1), A Firm’s System of Quality Management for Firms that Perform Audits or Reviews of Financial Statements, or Other Assurance or Related Services Engagements, paragraph 34(f).

² ~~ISQM 1, paragraph 34(f)~~ ² See footnote 1.

The Firm’s System of Quality Management and Role of Engagement Quality Reviews	
<p>5. ISQM<u>SQMS No.</u> 1 establishes the firm’s responsibilities for its system of quality management and requires the firm to design and implement responses to address the quality risks in a manner that is based on, and responsive to, the reasons for the assessments given to the quality risks.³ The specified responses in ISQM<u>SQMS No.</u> 1⁴ include establishing policies or procedures addressing engagement quality reviews in accordance with this ISQM<u>SQMS</u>.</p>	
<p>6. The firm is responsible for designing, implementing, and operating the system of quality management. Under ISQM<u>SQMS No.</u> 1, the objective of the firm is to design, implement, and operate a system of quality management for audits or reviews of financial statements, or other assurance or related services engagements performed by the firm, <u>in its accounting and auditing practice</u>⁵ that provides the firm with reasonable assurance that:</p>	Specific to U.S.
<p>a. the firm and its personnel fulfill their responsibilities in accordance with professional standards and applicable legal and regulatory requirements, and conduct engagements in accordance with such standards and requirements; and</p>	
<p>b. engagement reports issued by the firm or engagement partners are appropriate in the circumstances.⁴ ⁶</p>	
<p>7. As explained in ISQM<u>SQMS No.</u> 1,⁵ the public interest is served by the consistent performance of quality engagements. Quality engagements are achieved through planning and performing engagements and reporting on them in accordance with professional standards and applicable legal and regulatory requirements. Achieving the objectives of those standards and complying with the requirements of applicable law or regulation involves exercising professional judgment and, when applicable to the type of engagement, exercising<u>maintaining</u> professional skepticism.</p>	ASB preferred wording
<p>8. An engagement quality review is an objective evaluation of the significant judgments made by the engagement team and the conclusions reached thereon. The engagement quality reviewer’s evaluation of significant judgments is performed in the context of professional</p>	

³ ~~ISQM 1,~~ Paragraph ~~26~~25 of SQMS No. 1.

⁴ Paragraph 35f of SQMS No. 1.

⁵ The term *auditing and accounting practice* is defined in paragraph 17a of SQMS No. 1.

⁴ ~~ISQM 1, paragraph 14~~

⁶ Paragraph 15 of SQMS No. 1.

⁵ ~~ISQM 1, paragraph 15~~

<p>standards and applicable legal and regulatory requirements. However, an engagement quality review is not intended to be an evaluation of whether the entire engagement complies with professional standards and applicable legal and regulatory requirements⁷, or with the firm’s policies or procedures.</p>	
<p>9. The engagement quality reviewer is not a member of the engagement team. The performance of an engagement quality review does not change the responsibilities of the engagement partner for managing and achieving quality on the engagement⁷, or for the direction and supervision of the members of the engagement team and the review of their work. The engagement quality reviewer is not required to obtain evidence to support the opinion or conclusion on the engagement, but the engagement team may obtain further evidence in responding to matters raised during the engagement quality review.</p>	
<p>Authority of This ISQM <u>SQMS</u></p>	
<p>10. 40. This ISQM <u>SQMS</u> contains the objective for the firm in following this ISQM <u>SQMS</u> and requirements designed to enable the firm and the engagement quality reviewer to meet that stated objective. In addition, this ISQM <u>it</u> contains related guidance in the form of application and other explanatory material and introductory material that provides context relevant to a proper understanding of this ISQM <u>SQMS</u> and definitions. ISQMS <u>SQMS No. 1</u>^{6,7} explains the terms <i>objective</i>, <i>requirements</i>, <i>application material</i> and <i>other explanatory material</i>, <i>introductory material</i>, and <i>definitions</i>.</p>	
<p>Effective Date</p>	
<p>11. 41. This ISQM <u>SQMS</u> is effective for:</p>	
<p>a. audits and <u>or</u> reviews of financial statements for periods beginning on or after December 15, 2022 <u>2025</u>, and</p>	
<p>b. other assurance and related services engagements <u>in the firm’s accounting and auditing practice</u> beginning on or after December 15, 2022 <u>2025</u>.</p>	
<p>Objective</p>	
<p>12. The objective of the firm, through appointing an eligible engagement quality reviewer, is to perform an objective evaluation of the significant</p>	

⁶ ~~ISQM 1~~, ⁷ Paragraphs 12 and A6–A9 of SQMS No. 1.

<p>judgments made by the engagement team and the conclusions reached thereon.</p>	
<p>Definitions</p>	
<p>13. For purposes of this ISQM <u>the SQMSs</u>, the following terms have the meanings attributed below <u>as follows</u>:</p>	
<p>a. Engagement quality review— <u>3</u> An objective evaluation of the significant judgments made by the engagement team, and the conclusions reached thereon, performed by the engagement quality reviewer and completed on or before the date of the engagement report <u>is released</u>.</p>	<p>Difference in requirement (see par. 24b)</p>
<p>b. Engagement quality reviewer— <u>3</u> A partner, other individual in the firm, or an external individual, appointed by the firm to perform the engagement quality review.</p>	
<p>c. Relevant ethical requirements— <u>3</u> Principles of professional ethics and ethical requirements that are applicable to a professional accountant to which the engagement team and engagement quality reviewer, when undertaking the an engagement quality review. Relevant ethical requirements ordinarily comprise the provisions of the International Ethics Standards Board for Accountants' International, are subject, which consist of the AICPA Code of Ethics for Professional Accountants (including International Independence Standards) (IESBA Code) related to audits or reviews of financial statements, or other assurance or related services engagements, together with national requirements <u>Conduct together with rules of applicable state boards of accountancy and applicable regulatory agencies</u> that are more restrictive. (Ref: par. A 1211–A1514)</p>	<p>Specific to U.S.</p>
<p>Requirements</p>	
<p>Applying, and Complying With, Relevant Requirements</p>	
<p>14. The firm and the engagement quality reviewer shall <u>should</u> have an understanding of this ISQM <u>SQMS</u>, including the application and other explanatory material, to understand the objective of this ISQM <u>SQMS</u> and to properly apply the requirements relevant to them.</p>	<p>ASB preferred wording</p>
<p>15. The firm or the engagement quality reviewer, as applicable, shall <u>should</u> comply with each requirement of this ISQM <u>SQMS</u>, unless the requirement is not relevant in the circumstances of the engagement.</p>	
<p>16. The proper application of the requirements is expected to provide a sufficient basis for the achievement of the objective of this standard. However, if the firm or the engagement quality reviewer determines that the application of the relevant requirements does not provide a sufficient</p>	

<p>basis for the achievement of the objective of this standard, the firm or the engagement quality reviewer, as applicable, shall<u>should</u> take further actions to achieve the objective.</p>	
<p>Appointment and Eligibility of Engagement Quality Reviewers</p>	
<p>17. The firm shall<u>should</u> establish policies or procedures that require the assignment of responsibility for the appointment of engagement quality reviewers to an individual(s) <u>or individuals</u> with the competence, capabilities, and appropriate authority within the firm to fulfill the responsibility. Those policies or procedures shall<u>should</u> require such individual(s) <u>or individuals</u> to appoint the engagement quality reviewer. (Ref: par. A1–A3)</p>	<p>AICPA Style</p>
<p>18. The firm shall<u>should</u> establish policies or procedures that set forth the criteria for eligibility to be appointed as an engagement quality reviewer. Those policies or procedures shall<u>should</u> require that the engagement quality reviewer (Ref: par. A4)</p>	
<p>a. not be a member of the engagement team, and: (Ref: par. A4);</p>	
<p>b. Has<u>have</u> the competence and capabilities, including sufficient time, and the appropriate authority to perform the engagement quality review; (Ref: par. A5–A11<u>10</u>)</p>	
<p>c. Complies<u>comply</u> with relevant ethical requirements, including in relation to those <u>addressing</u> threats to <u>the</u> objectivity and independence of the engagement quality reviewer; and (Ref: par. A12<u>11</u>–A15<u>13</u>)</p>	
<p>d. Complies<u>comply</u> with provisions of law and regulation, if any, that are relevant to the eligibility of the engagement quality reviewer. (Ref: par. A16<u>14</u>)</p>	
<p>19. The firm's policies or procedures established in accordance with paragraph 18(b)<u>c</u> shall <u>should</u> also address threats to objectivity created by an individual being appointed as an<u>the</u> engagement quality reviewer after previously serving as the engagement partner. Such policies or procedures shall specify a cooling-off period of two years, or a longer period if required by relevant ethical requirements, before the engagement partner can assume the role of engagement quality reviewer. (Ref: par. A15–A17–A18)</p>	<p>The AICPA Code of Professional Conduct does not require engagement partner rotation, and ASB believes it would be inconsistent in the US to require a cooling-off period for</p>

	engagement quality reviewers but not engagement partner rotation.
20. The firm shall should establish policies or procedures that set forth the criteria for eligibility of individuals who assist the engagement quality reviewer. Those policies or procedures shall should require that such individuals	
a. not be members of the engagement team; and;	
b. have the competence and capabilities, including sufficient time, to perform the duties assigned to them; and (Ref: par. A 19 18)	
c. comply with relevant ethical requirements, including in relation to addressing threats to their objectivity and independence and, if applicable, the provisions of law and regulation. (Ref: par. A19–A20–A)	To clarify; no change in application intended
21. The firm shall should establish policies or procedures that:	
a. require the engagement quality reviewer to take overall responsibility for the performance of the engagement quality review; and	
b. address the engagement quality reviewer’s responsibility for determining the nature, timing, and extent of the direction and supervision of the individuals assisting in the <u>engagement quality review</u> ; and the review of their work. (Ref: par. A 22 21)	To clarify
<i>Impairment of the Engagement Quality Reviewer’s Eligibility to Perform the Engagement Quality Review</i>	
22. The firm shall should establish policies or procedures that address circumstances in which the engagement quality reviewer’s eligibility to perform the engagement quality review is impaired and the appropriate actions to be taken by the firm, including the process for identifying and appointing a replacement in such circumstances. (Ref: par. A22)	
23. When the engagement quality reviewer becomes aware of circumstances that impair the engagement quality reviewer’s eligibility, the engagement quality reviewer shall should notify the appropriate individual (s) or individuals in the firm; and; (Ref: par. A 24 23)	
a. if the engagement quality review has not commenced, decline the appointment to perform the engagement quality review; or	
b. if the engagement quality review has commenced, discontinue the performance of the engagement quality review.	

Performance of the Engagement Quality Review		
24.	The firm shall <u>should</u> establish policies or procedures regarding the performance of the engagement quality review that address <u>the following</u> :	
	a. The engagement quality reviewer’s responsibilities to perform procedures in accordance with paragraphs 25–26 at appropriate points in time during the engagement to provide an appropriate basis for an objective evaluation of the significant judgments made by the engagement team and the conclusions reached thereon;	
	b. The responsibilities of the engagement partner in relation to the engagement quality review, including that the engagement partner is precluded from dating <u>releasing</u> the engagement report until notification has been received from the engagement quality reviewer, in accordance with paragraph 27, that the engagement quality review is complete; and (Ref: par. A25 <u>24</u> –A26)	The ASB believes that the flexibility of using the report release date provides greater benefit than the logistical cost of restricting the time available for completing the engagement quality review.
	c. Circumstances when <u>in which</u> the nature and extent of engagement team discussions with the engagement quality reviewer about a significant judgment give rise to a threat to the objectivity of the engagement quality reviewer; and appropriate actions to take in these circumstances. (Ref: par. A27)	AICPA Style
25.	In performing the engagement quality review, the engagement quality reviewer shall <u>should do the following</u> : (Ref: par. A28–A33)	AICPA Style
	a. Read, and obtain an understanding of <u>about</u> , information communicated by: (Ref: par. A34)	AICPA Style
	i. the engagement team regarding the nature and circumstances of the engagement and the entity; and	
	ii. the firm related to the firm’s monitoring and remediation process, in particular, identified deficiencies that may relate to, or affect, the areas involving significant judgments made by the engagement team.	
	b. Discuss with the engagement partner and, if applicable, other members of the engagement team, significant matters and significant judgments made in planning, performing, and reporting on the engagement. (Ref: par. A35–A38)	

<p>c. Based on the information obtained in (a) and (b), review selected engagement documentation relating to the significant judgments made by the engagement team and evaluate <u>the following</u>: (Ref: par. A39–A43)</p>	<p>AICPA Style</p>
<p>i. The basis for making those significant judgments, including, when applicable to the type of engagement, the exercise<u>maintenance</u> of professional skepticism by the engagement team;</p>	<p>ASB preferred word</p>
<p>ii. Whether the engagement documentation supports the conclusions reached;and</p>	
<p>iii. Whether the conclusions reached are appropriate</p>	
<p>d. For audits of financial statements, Evaluate the basis for the engagement partner’s determination that relevant ethical requirements relating to independence, <u>when applicable</u>, have been fulfilled. (Ref: par. A44)</p>	<p>To apply to all engagements requiring independence</p>
<p>e. Evaluate whether appropriate consultation has taken place on difficult or contentious matters or matters involving differences of opinion and the conclusions arising from those consultations. (Ref: par. A45)</p>	
<p>f. For audits of financial statements<u>engagements conducted in accordance with generally accepted auditing standards</u>, evaluate the basis for the engagement partner’s determination that the engagement partner’s involvement has been sufficient and appropriate throughout the audit engagement such that the engagement partner has the<u>an appropriate</u> basis for determining that the significant judgments made and the conclusions reached are appropriate given the nature and circumstances of the engagement. (Ref: par. A46–<u>A47</u>)</p>	<p>To apply to all engagements To clarify; no change in application intended</p>
<p>g. Review:–</p>	
<p>i. for audits of financial statements, the financial statements and the auditor’s report thereon, including, if applicable, the description of the key audit matters; (Ref: par. A4748)</p>	
<p>ii. for review engagements<u>reviews</u> of financial statements or financial information, the financial statements or financial information and the engagement<u>review</u> report thereon; or (Ref: par. A4748)</p>	<p>To specify reviews under SASs or SSARS</p>
<p>iii. for other assurance and related services engagements, the engagement report, and when applicable, the subject matter information. (Ref: par. A48<u>49</u>)</p>	

<p>26. The engagement quality reviewer shall<u>should</u> notify the engagement partner if the engagement quality reviewer has concerns that the significant judgments made by the engagement team, <u>including the appropriate maintenance of professional skepticism by the engagement team when applicable to the type of engagement</u>, or the conclusions reached thereon, are not appropriate. If such concerns are not resolved to the engagement quality reviewer's satisfaction, the engagement quality reviewer shall<u>should</u> notify an<u>the</u> appropriate individual(s) <u>or individuals</u> in the firm that the engagement quality review cannot be completed. (Ref: par. A49<u>50</u>)</p>	<p>To emphasize the need for professional skepticism</p>
<p><i>Completion of the Engagement Quality Review</i></p>	
<p>27. The engagement quality reviewer shall<u>should</u> determine whether the requirements in this ISQM<u>SQMS</u> with respect to the performance of the engagement quality review have been fulfilled, and whether the engagement quality review is complete. If so, the engagement quality reviewer shall<u>should</u> notify the engagement partner that the engagement quality review is complete.</p>	
<p>Documentation</p>	
<p>28. The firm shall<u>should</u> establish policies or procedures that require the engagement quality reviewer to take responsibility for documentation of the engagement quality review. (Ref: par. A50<u>51</u>)</p>	
<p>29. The firm shall<u>should</u> establish policies or procedures that require documentation of the engagement quality review in accordance with paragraph 30, and <u>require</u> that such documentation be included with the engagement documentation.</p>	
<p>30. The engagement quality reviewer shall<u>should</u> determine that the documentation of the engagement quality review is sufficient to enable an experienced practitioner, having no previous connection with the engagement, to understand the nature, timing, and extent of the procedures performed by the engagement quality reviewer and, when applicable, individuals who assisted the reviewer, and <u>to understand</u> the conclusions reached in performing the review. The engagement quality reviewer <u>should</u> also shall determine that the documentation of the engagement quality review includes <u>the following</u>: (Ref: par. A54<u>52</u>–A53<u>54</u>)</p>	<p>To clarify; no change in application intended.</p>
<p>a. The names of the engagement quality reviewer and <u>any</u> individuals who assisted with the engagement quality review;</p>	<p>AICPA Style</p>
<p>b. An identification of the engagement documentation reviewed;</p>	
<p>c. The basis for the engagement quality reviewer's determination in accordance with paragraph 27;</p>	
<p>d. The notifications required in accordance with paragraphs 26 and 27;</p>	

and	
e. The date of completion of the engagement quality review;	

Application and Other Explanatory Material	
Appointment and Eligibility of Engagement Quality Reviewers	
<i>Assignment of Responsibility for the Appointment of Engagement Quality Reviewers (Ref: par. 17)</i>	
A1. Competence and capabilities that are relevant to an individual’s ability to fulfill responsibility for the appointment of the engagement quality reviewer may include appropriate knowledge about <u>the following</u> :	AICPA Style
<ul style="list-style-type: none"> • The responsibilities of an engagement quality reviewer; 	
<ul style="list-style-type: none"> • The criteria in paragraphs 18 and 19 regarding the eligibility of engagement quality reviewers; and 	AICPA Style
<ul style="list-style-type: none"> • The nature and circumstances of the engagement or the entity subject to an engagement quality review, including the composition of the engagement team. 	
A2. The firm’s policies or procedures may specify that the individual responsible for the appointment of engagement quality reviewers not be a member of the engagement team for which an engagement quality review is to be performed. However, in certain circumstances (e.g. for example , in the case of a smaller firm or a sole practitioner), it may not be practicable for an individual other than a member of the engagement team to appoint the engagement quality reviewer.	AICPA Style
A3. The firm may assign more than one individual to be responsible for appointing engagement quality reviewers. For example, the firm’s policies or procedures may specify a different process for appointing engagement quality reviewers for audits of listed entities <u>financial statements</u> than for audits of non-listed entities <u>attestation examination engagements</u> or other engagements, with different individuals responsible for each process.	Specific to ASB’s jurisdiction.
<i>Eligibility of the Engagement Quality Reviewer (Ref: par. 18)</i>	
A4. In some circumstances, for example, in the case of a smaller firm or a sole practitioner, there may not be a partner or other individual in the firm who is eligible to perform the engagement quality review. In these circumstances, the firm may contract with, or obtain the services of, individuals external to the firm to perform the engagement quality	

<p>review. An individual external to the firm may be a partner or an employee of a network firm, a structure or an organization within the firm’s network, or a service provider. When using such an individual, the provisions in ISQM<u>SQMS No.</u> 1 addressing network requirements or network services or service providers apply.</p>	
<p><i>Eligibility Criteria for the Engagement Quality Reviewer</i></p>	
<p><i>Competence and Capabilities, Including Sufficient Time (Ref: par. 18(a))</i></p>	
<p>A5. SQMS No.<u>ISQM</u> 1 describes characteristics related to competence, including the integration and application of technical competence, professional skills, and professional ethics, values, and attitudes.^{7,8} Matters<u>Characteristics</u> that the firm may consider in determining that an individual has the necessary competence to perform an engagement quality review include, for example, <u>the following</u>:</p>	<p>To clarify; no change in application intended.</p>
<ul style="list-style-type: none"> • An understanding of professional standards and applicable legal and regulatory requirements and of the firm’s policies or procedures relevant to the engagement; 	
<ul style="list-style-type: none"> • Knowledge of the entity’s industry; 	
<ul style="list-style-type: none"> • An understanding of, and experience relevant to, engagements of a similar nature and complexity; and 	
<ul style="list-style-type: none"> • An understanding of the responsibilities of the engagement quality reviewer in performing and documenting the engagement quality review, which may be attained or enhanced by receiving relevant training from the firm. 	
<p>A6. The conditions, events, circumstances, actions, or inactions considered by the firm in determining that an engagement quality review is an appropriate response to address one or more quality risk(s)⁹<u>risks</u> may be an important consideration in<u>to</u> the firm’s determination of the competence and capabilities required to perform the engagement quality review for that engagement. Other considerations that the firm may take into account in determining whether the engagement quality reviewer has the competence and capabilities, including sufficient time, needed to evaluate the significant judgments made by the engagement team and the conclusions reached thereon include, for example, <u>the following</u>:</p>	<p>To clarify; no change in application intended.</p>
<ul style="list-style-type: none"> • The nature of the entity; 	
<ul style="list-style-type: none"> • The specialization and complexity of the industry or regulatory environment in which the entity operates. 	

⁷-ISQM 1, ⁸ Paragraph A8892 of SQMS No. 1.

⁸-ISQM 1, paragraph A134⁹ See footnote 8.

<ul style="list-style-type: none"> The extent to which the engagement relates to matters requiring specialized expertise (e.g. for example, with respect to information technology (IT) or specialized areas of accounting or auditing), or scientific and engineering expertise, such as <u>which</u> may be needed for certain assurance engagements. (Also see paragraph A19. A7.) 	AICPA Style
<p>A7. In evaluating the competence and capabilities of an individual who may be appointed as an engagement quality reviewer, the findings arising from the firm’s monitoring activities (e.g. for example, findings from the inspection of engagements for which the individual was an engagement team member or engagement quality reviewer) or the results of external inspections may also be relevant considerations.</p>	AICPA Style
<p>A8. A lack of appropriate competence or capabilities affects the ability of the engagement quality reviewer to exercise appropriate professional judgment in performing the review. For example, an engagement quality reviewer who lacks relevant industry experience may not possess the ability or confidence necessary to evaluate and, where <u>when</u> appropriate, challenge significant judgments made, and the exercise <u>maintenance</u> of professional skepticism, by the engagement team on a complex, industry-specific accounting or auditing matter.</p>	Preferred wording
<p><i>Appropriate Authority (Ref: par. 18(a))</i></p>	
<p>A9. Actions at the firm level help to establish the authority of the engagement quality reviewer. For example, by creating <u>when the firm has created</u> a culture of respect for the role of the engagement quality reviewer, the engagement quality reviewer is less likely to experience pressure from the engagement partner or other personnel to inappropriately influence the outcome of the engagement quality review. In some cases, the engagement quality reviewer’s authority may be enhanced by the firm’s policies or procedures to address differences of opinion, which may include actions the engagement quality reviewer may take when a disagreement occurs between the engagement quality reviewer and the engagement team.</p>	To clarify; no change in application intended.
<p>A10. The authority of the engagement quality reviewer may be diminished when:</p>	
<ul style="list-style-type: none"> the culture within the firm promotes respect for authority only of <u>for</u> personnel at a higher level of hierarchy within the firm. 	AICPA Style
<ul style="list-style-type: none"> the engagement quality reviewer has a reporting line to the engagement partner, for example, when the engagement partner holds a leadership position in the firm or is responsible for determining the compensation of the engagement quality reviewer. 	
<p>Public Sector Considerations</p>	

<p>A11. In the public sector, an auditor (e.g., an Auditor General, or other suitably qualified individual appointed on behalf of the Auditor General) may act in a role equivalent to that of the engagement partner with overall responsibility for public sector audits. In such circumstances, the selection of the engagement quality reviewer may include consideration of the need for independence and the ability of the engagement quality reviewer to provide an objective evaluation.</p>	<p>Not applicable in U.S.</p>
<p><i>Relevant Ethical Requirements (Ref: par. 13(c), and 18(b))</i></p>	
<p>A11.A12. The relevant ethical requirements that are applicable when undertaking an engagement quality review may vary, depending on the nature and circumstances of the engagement or the entity. Various provisions of relevant ethical requirements may apply only to an individual professional accountants, such as an engagement quality reviewer, and not the firm itself.</p>	<p>“Professional accountant” is not a term used in the U.S.</p>
<p>A13. Relevant ethical For example, if a firm uses an external provider to perform an engagement quality review, that individual may be subject to independence requirements may include specific; however, the independence requirements imposed on that would apply to individual professional accountants, such as an engagement quality reviewer. Relevant ethical requirements may also include provisions that address threats to independence created by long association with an audit or assurance client. The application of any such provisions dealing with long association is distinct from, but may need to be taken into consideration in applying, the required cooling-off period in accordance with paragraph 19 as a result of performing the engagement quality review may not extend to the entire firm for which that individual works.</p>	<p>To make specific to the U.S.</p>
<p>Threats to the Objectivity of the Engagement Quality Reviewer</p>	
<p>A12. A14. Threats to the engagement quality reviewer’s objectivity may be created by a broad range of facts and circumstances. For example Examples follow:</p>	
<ul style="list-style-type: none"> • A self-review threat may be created when the engagement quality reviewer previously was involved with significant judgments made by the engagement team, in particular, as the engagement partner or other another engagement team member. 	
<ul style="list-style-type: none"> • A familiarity or self-interest threat may arise when the engagement quality reviewer is a close or immediate family member of the engagement partner or another member of the engagement team, or through close personal relationships with members of the engagement team. 	

<ul style="list-style-type: none"> An intimidation threat may be created when actual or perceived pressure is exerted on the engagement quality reviewer (e.g. for example, when the engagement partner is an aggressive or dominant individual, or the engagement quality reviewer has a reporting line to the engagement partner). 	
<p>A13.A15. Relevant ethical requirements may include requirements and guidance to identify, evaluate, and address threats to objectivity. For example, the IESBA Code provides specific guidance, including examples of:</p> <ul style="list-style-type: none"> Circumstances where <u>They may also include provisions that address</u> threats to objectivity may be <u>independence</u> created when a professional accountant is appointed as an engagement quality reviewer; Factors that are relevant in evaluating the level of such threats; and Actions, including safeguards, that might address such threats <u>by long association with an audit or assurance client.</u> 	<p>To make specific to the U.S.</p>
<p><i>Law or Regulation Relevant to the Eligibility of the Engagement Quality Reviewer (Ref: par. 18(c))</i></p>	
<p>A14.A16. Law or regulation may prescribe additional requirements regarding the eligibility of the engagement quality reviewer. For example, in some jurisdictions, <u>the audit requirements of the FDIC regulations for certain financial institutions require the auditor (which includes the engagement quality reviewer may need) to possess certain qualifications or be licensed to be able to perform the engagement quality review</u> <u>be in compliance with the AICPA's Code of Professional Conduct and also meet the independence requirements and interpretations of the SEC and its staff.</u></p>	<p>To make specific to the U.S.</p>
<p>Cooling-Off Period for an Individual After Previously Serving as <u>Considerations Related to Assigning the Previous Engagement Partner as Engagement Quality Reviewer</u> (Ref: par. 19)</p>	<p>See par. 19</p>
<p>A15.A17. In recurring engagements, the matters on which significant judgments are made often do not vary. Therefore, significant judgments made in prior periods may continue to affect judgments of the engagement team in subsequent periods. <u>Therefore,</u> the ability of an engagement quality reviewer to perform an objective evaluation of significant judgments is therefore affected when the individual was previously involved with those judgments as the engagement partner. In such circumstances, it is important that appropriate safeguards are put in place to reduce threats to objectivity, in particular, the self-review threat, to an acceptable level. Accordingly, this ISQM requires the firm to establish <u>The following factors may be taken into consideration when</u></p>	<p>The ASB has added application materials addressing the objectivity of EQRs in the absence of a requirement for a cooling-off period.</p>

<p><u>designing</u> policies or <u>and</u> procedures that specify to <u>maintain the objectivity of an engagement quality reviewer who served as the engagement partner on the previous year’s engagement:</u></p>	
<ul style="list-style-type: none"> • <u>The extent of changes in the matters on which significant judgments are made and the facts and circumstances around those significant judgments compared to the period or periods in which the individual was the engagement partner. For example, if a business combination with a material effect on the financial statements or key management personnel changes have occurred, the significant judgments made in the current period may vary from those of the prior period to such an extent that an objective evaluation of those judgments could be made by the individual who served as the engagement partner in the previous period.</u> 	
<ul style="list-style-type: none"> • <u>The procedures and incentives placed by the firm’s system of quality management on objective reviews (for example, whether the firm has a culture of accountability that focuses on improving identified deficiencies or a culture of blame that focuses on penalizing people).</u> 	
<p><u>A firm may establish policies or procedures that limit the eligibility to be appointed as engagement quality reviewers of individuals who previously served as the engagement partner, for example, by establishing a specified cooling-off period during which the engagement partner is precluded from being appointed as the engagement quality reviewer. Determining a suitable cooling-off period depends on the facts and circumstances of the engagement.</u></p>	
<p>A16.A18 The firm’s policies or procedures also may <u>also</u> address whether a cooling-off period is appropriate for an individual other than the engagement partner before becoming eligible to be appointed as the engagement quality reviewer on that engagement. In this regard, the firm may consider the nature of that individual’s role and previous involvement with the significant judgments made on the engagement. For example, the firm may determine that an engagement partner responsible for the performance of audit procedures on the financial information of a component in a group audit engagement may not be eligible to be appointed as the group engagement quality reviewer because of that audit partner’s involvement in the significant judgments affecting the group audit engagement.</p>	
<p><i>Circumstances When in Which the Engagement Quality Reviewer Uses Assistants (Ref: par. 20–21)</i></p>	
<p>A17.A19– In certain circumstances, it may be appropriate for the engagement quality reviewer to be assisted by an individual or team of individuals with the relevant expertise. For example, <u>assistance from individuals with</u> highly specialized knowledge, skills, or expertise may be useful for understanding</p>	

<p>certain transactions undertaken by the entity to help the engagement quality reviewer evaluate the significant judgments made by the engagement team related to those transactions.</p>	
<p>A18.A20— The guidance in paragraph A14 may be helpful to the firm when establishing policies or procedures that address threats to objectivity of individuals who assist the engagement quality reviewer.</p>	
<p>A19.A21— When the engagement quality reviewer is assisted by an individual external to the firm, the assistant’s responsibilities, including those related to compliance with relevant ethical requirements, may be set out in the contract or other agreement between the firm and the assistant.</p>	
<p>A20.A22— The firm’s policies or procedures may include responsibilities of the engagement quality reviewer to:</p>	
<ul style="list-style-type: none"> • consider whether assistants understand their instructions and whether the work is being carried out in accordance with the planned approach to the engagement quality review; and 	
<ul style="list-style-type: none"> • address matters raised by assistants, considering their significance and modifying the planned approach appropriately. 	
<p><i>Impairment of the Engagement Quality Reviewer’s Eligibility to Perform the Engagement Quality Review (Ref: par. 22–23)</i></p>	
<p>A21.A23— Factors that may be relevant to the firm in considering whether the eligibility of the engagement quality reviewer to perform the engagement quality review is impaired include <u>the following</u>:</p>	
<ul style="list-style-type: none"> • Whether changes in the circumstances of the engagement result in the engagement quality reviewer no longer having the appropriate competence and capabilities to perform the review; 	
<ul style="list-style-type: none"> • Whether changes in the other responsibilities of the engagement quality reviewer indicate that the individual no longer has sufficient time to perform the review; or 	
<ul style="list-style-type: none"> • Notification from the engagement quality reviewer in accordance with paragraph 23. 	
<p>A22.A24— In circumstances in which the engagement quality reviewer’s eligibility to perform the engagement quality review becomes impaired, the firm’s policies or procedures may set out a process by which alternative eligible individuals are identified. The firm’s policies or procedures may also address the responsibility of the individual appointed to replace the engagement quality reviewer to perform procedures sufficient to fulfill the requirements of this ISQM<u>SQMS</u> with respect to the performance of the engagement quality review. Such</p>	

<p>policies or procedures may further address the need for consultation in such circumstances- <u>and may include, for example, the following:</u></p>	
<ul style="list-style-type: none"> • <u>Evaluation of whether procedures performed by the previous engagement quality reviewer could be relied on by the newly assigned engagement quality reviewer or whether all work would need to be reperformed</u> 	<p>Additional guidance</p>
<ul style="list-style-type: none"> • <u>Consideration of the effect of an engagement quality review assistant on the transition, when such assistant has been involved in the engagement quality review prior to transition</u> 	
<ul style="list-style-type: none"> • <u>Procedures undertaken by the engagement team to inform the newly assigned engagement quality reviewer about planning meeting discussions that have already occurred and other matters in which the previous engagement quality reviewer had been involved</u> 	
<ul style="list-style-type: none"> • <u>Documentation of the circumstances necessitating the change</u> 	
<p>Performance of the Engagement Quality Review (Ref: par. 24–27)</p>	
<p><i>Engagement Partner Responsibilities in Relation to the Engagement Quality Review (Ref: par. 24(b))</i></p>	
<p>A23.A25-ISA-220 (Revised)⁹ <u>Statement on Auditing Standards (SAS) No. 146, <i>Quality Management for an Engagement Conducted in Accordance With Generally Accepted Auditing Standards</i>¹⁰</u> establishes the requirements for the engagement partner in audit engagements for which an engagement quality review is required, including <u>the following:</u></p>	
<ul style="list-style-type: none"> • Determining that an engagement quality reviewer has been appointed; 	
<ul style="list-style-type: none"> • Cooperating with the engagement quality reviewer and informing other members of the engagement team of their responsibility to do so; 	
<ul style="list-style-type: none"> • Discussing significant matters and significant judgments arising during the audit engagement, including those identified during the engagement quality review, with the engagement quality reviewer; and 	
<ul style="list-style-type: none"> • Not dating <u>releasing</u> the auditor’s report until the completion of the engagement quality review. 	

⁹ International Standard on Auditing (ISA) 220 (Revised), *Quality Management for an Audit of Financial Statements*, paragraph 36

¹⁰ Paragraph 36 of *Statement on Auditing Standards (SAS) No. 146, Quality Management for an Engagement Conducted in Accordance With Generally Accepted Auditing Standards*.

<p>A24. <u>Professional standards require that the engagement report not be dated earlier than the date on which sufficient appropriate engagement evidence has been obtained. If the engagement quality review is completed after the report is dated and identifies instances in which the report was dated before sufficient appropriate engagement evidence has been obtained, the date of the report is required to be changed to the date when the additional evidence has been obtained. Such instances, if not rare, may be indicative of a deficiency or deficiencies in the firm’s system of quality management.</u></p>	<p>Additional guidance</p>
<p>A25.A26. ISAE 3000 (Revised)⁴⁰ <u>AT-C section 105, Concepts Common to All Attestation Engagements,</u>^{11*} also establishes requirements for the engagement partner in relation to the engagement quality review.</p>	
<p><i>Discussions Between the Engagement Quality Reviewer and the Engagement Team (Ref: par. 24(c))</i></p>	
<p>A26. A27. Frequent communication between the engagement team and engagement quality reviewer throughout the engagement may assist in facilitating an effective and timely engagement quality review. However, a threat to the objectivity of the engagement quality reviewer may be created depending on the timing and extent of the discussions with the engagement team about a significant judgment. The firm’s policies or procedures may set out the actions to be taken by the engagement quality reviewer or the engagement team to avoid situations in which the engagement quality reviewer is, or may be perceived to be, making decisions on behalf of the engagement team. For example, in these circumstances, the firm may require consultation about such significant judgments with other relevant personnel in accordance with the firm’s consultation policies or procedures.</p>	
<p><i>Procedures Performed by the Engagement Quality Reviewer (Ref: par. 25–27)</i></p>	
<p>A27.A28. The firm’s policies or procedures may specify the nature, timing, and extent of the procedures performed by the engagement quality reviewer and also may emphasize the importance of the engagement quality reviewer exercising professional judgment in performing the review.</p>	

⁴⁰¹¹ Paragraph 36 of International Standard on Assurance Engagements (ISAE) 3000 (Revised), Assurance Engagements Other than Audits or Reviews of Historical Financial Information,~~paragraph 36.~~

* All AT-C sections can be found in AICPA Professional Standards.

<p>A28. A29. The timing of the procedures performed by the engagement quality reviewer may depend on the nature and circumstances of the engagement or the entity, including the nature of the matters subject to the review. Timely review of the engagement documentation by the engagement quality reviewer throughout all stages of the engagement (e.g. for example, planning, performing, and reporting) allows matters to be promptly resolved to the engagement quality reviewer’s satisfaction, or before the date <u>release</u> of the engagement report. For example, the engagement quality reviewer may perform procedures in relation to the overall strategy and plan for the engagement at the completion of the planning phase. Timely performance of the engagement quality review <u>may</u> also may reinforce the exercise of professional judgment and, when applicable to the type of engagement, <u>maintenance of</u> professional skepticism, by the engagement team in planning and performing the engagement.</p>	
<p>A29. A30.— The nature and extent of the engagement quality reviewer’s procedures for a specific engagement may depend on <u>the following</u>, among other factors:</p>	
<ul style="list-style-type: none"> • The reasons for the assessments given to quality risks,⁴⁴¹² for example, engagements performed for entities in emerging industries or with complex transactions. 	
<ul style="list-style-type: none"> • Identified deficiencies, and the remedial actions to address the identified deficiencies, related to the firm’s monitoring and remediation process, and any related guidance issued by the firm, which may indicate areas where more extensive procedures need to be performed by the engagement quality reviewer. 	
<ul style="list-style-type: none"> • The complexity of the engagement. 	
<ul style="list-style-type: none"> • The nature and size of the entity, including whether the entity is a listed entity. 	
<ul style="list-style-type: none"> • Findings relevant to the engagement, such as the results of inspections undertaken by an external oversight authority in a prior period, or other concerns raised about the quality of the work of the engagement team. 	
<ul style="list-style-type: none"> • Information obtained from the firm’s acceptance and continuance of client relationships and specific engagements. 	
<ul style="list-style-type: none"> • For assurance engagements, the engagement team’s identification and assessment of, and responses to, risks of material misstatement in the engagement. 	

⁴⁴ ISQM 1, paragraph A49

¹² Paragraph A49 of SQMS No. 1.

<ul style="list-style-type: none"> • Whether members of the engagement team have cooperated with the engagement quality reviewer. The firm’s policies or procedures may address the actions the engagement quality reviewer takes in circumstances when<u>in which</u> the engagement team has not cooperated with the engagement quality reviewer, for example, informing an appropriate individual in the firm so appropriate action can be taken to resolve the issue. 	
<p>A30.<u>A31.</u> The nature, timing, and extent of the engagement quality reviewer’s procedures may need to change based on circumstances encountered in performing the engagement quality review.</p>	
<p><i>Group Audit Considerations</i></p>	
<p>A31.<u>A32.</u> The performance of an engagement quality review for an audit of group financial statements may involve additional considerations for the individual appointed as the engagement quality reviewer for the group audit, depending on the size and complexity of the group. Paragraph 21(a) requires the firm’s policies or procedures to require the engagement quality reviewer to take overall responsibility for the performance of the engagement quality review. In doing so, for larger and more complex group audits, the group engagement quality reviewer may need to discuss significant matters and significant judgments with key members of the engagement team other than the group engagement team (e-g<u>for example</u>, those responsible for performing audit procedures on the financial information of a component). In these circumstances, the engagement quality reviewer may be assisted by individuals in accordance with paragraph 20. The guidance in paragraph A22 may be helpful when the engagement quality reviewer for the group audit is using assistants.</p>	
<p>A32. <u>A33.</u> In some cases, an engagement quality reviewer may be appointed for an audit of an entity or business unit that is part of a group, for example, when such an audit is required by law, regulation, or <u>for</u> other reasons. In these circumstances, communication between the engagement quality reviewer for the group audit and the engagement quality reviewer for the audit of that entity or business unit may help the group engagement quality reviewer in fulfilling the responsibilities in accordance with paragraph 21(a). For example, this may be the case when the entity or business unit has been identified as a component for purposes of the group audit and significant judgments related to the group audit have been made at the component level.</p>	

<p><i>Information Communicated by the Engagement Team and the Firm (Ref: par- 25(a))</i> 25(a) <u>25a)</u></p>	
<p>A33.A34. Obtaining an understanding of information communicated by the engagement team and the firm in accordance with paragraph 25(a) may assist the engagement quality reviewer in understanding the significant judgments that may be expected for the engagement. Such an understanding may also provide the engagement quality reviewer with a basis for discussions with the engagement team about the significant matters and significant judgments made in planning, performing, and reporting on the engagement. For example, a deficiency identified by the firm may relate to significant judgments made by other engagement teams for certain accounting estimates for a particular industry. When this is the case, such information may be relevant to the significant judgments made on the engagement with respect to those accounting estimates, and, therefore, may provide the engagement quality reviewer with a basis for discussions with the engagement team in accordance with paragraph 25(b).</p>	
<p><i>Significant Matters and Significant Judgments (Ref: par. 25(b))</i> 25(c)</p>	
<p>A34.A35. For audits of financial statements, ISA 220 (Revised)⁴² <u>SAS No. 146</u>¹³ requires the engagement partner to review audit documentation relating to significant matters⁴³¹⁴ and significant judgments, including those relating to difficult or contentious matters identified during the engagement, and the conclusions reached.</p>	
<p>A35.A36. For audits of financial statements, ISA 220 (Revised)⁴⁴ <u>SAS No. 146</u>¹⁵ provides examples of significant judgments that may be identified by the engagement partner related to the overall audit strategy and audit plan for undertaking the engagement, the execution of the engagement, and the overall conclusions reached by the engagement team.</p>	
<p>A36.A37. For engagements other than audits of financial statements, the significant judgments made by the engagement team may depend on the nature and circumstances of the engagement or the entity. For example,</p>	

⁴² ~~ISA 220 (Revised), paragraph 31~~

¹³ Paragraph 31 of SAS No. 146.

⁴³ ~~ISA 230, Audit Documentation, paragraph 8(c)~~

¹⁴ Paragraph .08c of AU-C section 230, Audit Documentation. All AU-C sections can be found in AICPA Professional Standards.

⁴⁴ ~~ISA 220 (Revised), paragraph A93~~

¹⁵ Paragraph A93 of SAS No. 146.

<p>in an assurance<u>attestation</u> engagement performed in accordance with ISAE—3000—(Revised)<u>Statements on Standards for Attestation Engagements</u>, the engagement team’s determination of whether the criteria to be applied in the preparation of the subject matter information are suitable for the engagement may involve or require significant judgment.</p>	
<p>A37. A38.— In performing the engagement quality review, the engagement quality reviewer may become aware of other areas where significant judgments would have been expected to be made by the engagement team for which further information may be needed about the engagement team’s procedures performed or the basis for conclusions reached. In those circumstances, discussions with the engagement quality reviewer may result in the engagement team concluding that additional procedures need to be performed.</p>	
<p>A38. A39.— The information obtained in accordance with paragraphs 25(a) and 25(—b), and the review of selected engagement documentation, assists the engagement quality reviewer in evaluating the engagement team’s basis for making the significant judgments. Other considerations that may be relevant to the engagement quality reviewer’s evaluation include, for example, <u>the following</u>:</p>	
<ul style="list-style-type: none"> • Remaining alert to changes in the nature and circumstances of the engagement or the entity that may result in changes in the significant judgments made by the engagement team; 	
<ul style="list-style-type: none"> • Applying an unbiased view in evaluating responses from the engagement team;and 	
<ul style="list-style-type: none"> • Following up on inconsistencies identified in reviewing engagement documentation; or inconsistent responses by the engagement team to questions relating to the significant judgments made. 	
<p>A39. A40.— The firm’s policies or procedures may specify engagement documentation to be reviewed by the engagement quality reviewer. In addition, such policies or procedures may indicate that the engagement quality reviewer exercises professional judgment in selecting additional engagement documentation to be reviewed relating to significant judgments made by the engagement team.</p>	
<p>A40. A41.— Discussions about significant judgments with the engagement partner; and <u>if applicable</u>, other members of the engagement team, together with the engagement team’s documentation, may assist the engagement quality reviewer in evaluating the exercise<u>maintenance</u> of professional skepticism, when applicable to the engagement, by the engagement team in relation to those significant judgments.</p>	

<p>A41. A42.— For audits of financial statements, ISA 220 (Revised)¹⁵ SAS No. 146¹⁶ provides examples of the impediments to the exercisemaintenance of professional skepticism at the engagement level, unconscious auditor biases that may impede the exercisemaintenance of professional skepticism, and possible actions that the engagement team may take to mitigate impediments to the exercisemaintenance of professional skepticism at the engagement level.</p>	
<p>A42. A43.— For audits of financial statements, the requirements and relevant application material in ISA AU-C section 315 (Revised 2019),¹⁶ ISA 540 (Revised)¹⁷, Understanding the Entity and Its Environment and Assessing the Risks of Material Misstatement,¹⁷ AU-C section 540, Auditing Accounting Estimates and Related Disclosures,¹⁸ and other ISAsAU-C sections also provide examples of areas in an audit where the auditor exercisesmaintains professional skepticism, or examples of where appropriate documentation may help provide evidence about how the auditor exercisedmaintained professional skepticism. Such guidance may also assist the engagement quality reviewer in evaluating the exercisemaintenance of professional skepticism by the engagement team.</p>	
<p><i>Whether Relevant Ethical Requirements Relating to Independence Have Been Fulfilled (Ref: par. 25(d))</i></p>	
<p>A43. A44 SAS No. ISA 220 (Revised)¹⁸ 146¹⁹ requires the engagement partner, prior to dating the auditor’s report, to take responsibility for determining whether relevant ethical requirements, including those related to independence, have been fulfilled.</p>	

¹⁵ ~~ISA 220 (Revised)~~, paragraphs A34-A36

¹⁶ [Paragraphs A33–A35 of SAS No. 146.](#)

¹⁶ ~~ISA 315 (Revised 2019)~~, *Identifying and Assessing the Risks of Material Misstatement*, paragraph A238

¹⁷ ~~ISA 540 (Revised)~~, *Auditing Accounting Estimates and Related Disclosures*, paragraph A11

¹⁷ [Paragraph A255 of AU-C section 315, *Understanding the Entity and Its Environment and Assessing the Risks of Material Misstatement*.](#)

¹⁸ [Paragraph A11 of AU-C section 540, *Auditing Accounting Estimates and Related Disclosures*.](#)

¹⁸ ~~ISA 220 (Revised)~~, paragraph 21

¹⁹ [Paragraph 21 of SAS No. 146.](#)

<p><i>Whether Consultation Has Taken Place on Difficult or Contentious Matters or Matters Involving Differences of Opinion (Ref: par. 25(e))</i></p>	
<p>A44.A45 SQMS No. ISQM-1¹⁹²⁰ addresses consultation on difficult or contentious matters and differences of opinion within the engagement team, or between the engagement team and the engagement quality reviewer or individuals performing activities within the firm’s system of quality management.</p>	
<p>Sufficient and Appropriate Involvement of the Engagement Partner on the Engagement (Ref: par. 25(f))</p>	
<p>A45.A46 SAS No. ISA-220 (Revised)²⁰146²¹ requires the engagement partner to determine, prior to dating the auditor’s report, that the engagement partner’s involvement has been sufficient and appropriate throughout the audit engagement such that the engagement partner has the basis for determining that the significant judgments made and the conclusions reached are appropriate given the nature and circumstances of the engagement. ISA-220 (Revised)²⁴SAS No. 146²² also indicates that the documentation of the involvement of the engagement partner may be accomplished in different ways. Discussions with the engagement team, and review of such engagement documentation, may assist the engagement quality reviewer’s evaluation of the basis for the engagement partner’s determination that the engagement partner’s involvement has been sufficient and appropriate.</p>	
<p>A46. SAS No. 146 is adapted, as necessary, to engagements performed in accordance with generally accepted auditing standards other than audits of financial statements. Accordingly, the requirement in paragraph 25f is applicable to those engagements.</p>	
<p>Engagement Quality Reviewer’s Review of Financial Statements and Engagement Reports (Ref: par. 25(g))</p>	
<p>A47. For audits of financial statements, the engagement quality reviewer’s review of the financial statements and auditor’s report thereon may include consideration of whether the presentation and disclosure of matters relating to the significant judgments made by the engagement team are is</p>	

¹⁹ ISQM 1, paragraphs 31(d), 31(e) and A79-A82

²⁰ [Paragraphs 32d-e and A80-A83 of SQMS No. 1.](#)

²⁰ [ISA 220 \(Revised\), paragraph 40\(a\)](#)

²¹ [Paragraph 40a of SAS No. 146.](#)

²⁴ [ISA 220 \(Revised\), paragraph A119](#)

<p>consistent with the engagement quality reviewer’s understanding of those matters based on the review of selected engagement documentation, and discussions with the engagement team. In reviewing the financial statements, the engagement quality reviewer may also become aware of other areas where significant judgments would have been expected to be made by the engagement team for which further information may be needed about the engagement team’s procedures or conclusions. The guidance in this paragraph also applies to review engagements,<u>reviews of financial statements</u> and the related engagement report.</p>	
<p>A48. For other assurance and related services engagements <u>other than audits or reviews of financial statements</u>, the engagement quality reviewer’s review of the engagement report and, when applicable, the subject matter information may include considerations similar to those described in paragraph A47<u>46</u> (e.g. for example, whether the presentation or description of matters relating to the significant judgments made by the engagement team are consistent with the engagement quality reviewer’s understanding based on the procedures performed in connection with the <u>engagement quality</u> review).</p>	
<p>Unresolved Concerns of the Engagement Quality Reviewer (Ref: par. 26)</p>	
<p>A49. The firm’s policies or procedures may specify the individual(s) <u>or individuals</u> in the firm to be notified if the engagement quality reviewer has unresolved concerns that the significant judgments made by the engagement team, or the conclusions reached thereon, are not appropriate. Such individual(s)<u>individuals</u> may include the individual assigned the responsibility for the appointment of engagement quality reviewers. With respect to such unresolved concerns, the firm’s policies or procedures may also require consultation within or outside the firm (e.g. for example, a professional or regulatory body).</p>	
<p>Documentation (Ref: par. 28–30)</p>	
<p>A50. Paragraphs 57 to 60<u>58–61</u> of ISQM<u>SQMS No.</u> 1 address the firm’s documentation of its system of quality management. An engagement quality review performed in accordance with this ISQM is therefore subject to the, <u>which includes the firm’s policies and procedures addressing engagements that are required to be subject to engagement quality reviews. This SQMS addresses additional</u> documentation requirements in ISQM 1<u>related to such policies and procedures as well as documentation requirements related to the performance of engagement quality reviews undertaken at the engagement level.</u></p>	<p>Additional guidance</p>
<p>A51. The form, content, and extent of the documentation of the engagement quality review may depend on <u>the following</u> factors such as:</p>	

<ul style="list-style-type: none"> • The nature and complexity of the engagement; 	
<ul style="list-style-type: none"> • The nature of the entity; 	
<ul style="list-style-type: none"> • The nature and complexity of the matters subject to the engagement quality review; and 	
<ul style="list-style-type: none"> • The extent of the engagement documentation reviewed. 	
<p>A52. The performance and notification of the completion of the engagement quality review may be documented in a number of ways. For example, the engagement quality reviewer may document the review of engagement documentation electronically in the IT application for the performance of the engagement. Alternatively, the engagement quality reviewer may document the review through means of a memorandum. The engagement quality reviewer’s procedures may also be documented in other ways, for example, in the minutes of the engagement team’s discussions where<u>when</u> the engagement quality reviewer was present.</p>	
<p>A53. Paragraph 24(b) requires that the firm’s policies or procedures preclude the engagement partner from dating<u>releasing</u> the engagement report until the completion of the engagement quality review, which includes resolving matters raised by the engagement quality reviewer. Provided that all requirements with respect to the performance of the engagement quality review have been fulfilled, the documentation of the review may be finalized after the date<u>release</u> of the engagement report, but before the assembly of the final engagement file. However, firm policies or procedures may specify that the documentation of the engagement quality review needs to be finalized on or before the date of the engagement report.</p>	<p>Last sentence deleted so as not to be considered an implicit requirement.</p>

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Document 2 ID	2B SQMS 2 marked from January ASB Meeting.docx
Description	2B SQMS 2 marked from January ASB Meeting
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**~~INTERNATIONAL STANDARD~~ STATEMENT ON AUDITING
~~220~~ STANDARDS No. 146, **QUALITY MANAGEMENT FOR AN ~~AUDIT OF~~
~~FINANCIAL STATEMENTS~~ ENGAGEMENT CONDUCTED IN
ACCORDANCE WITH GENERALLY ACCEPTED AUDITING
STANDARDS****

~~(Effective for audits of financial statements for periods beginning
on or after December 15, 2022)~~

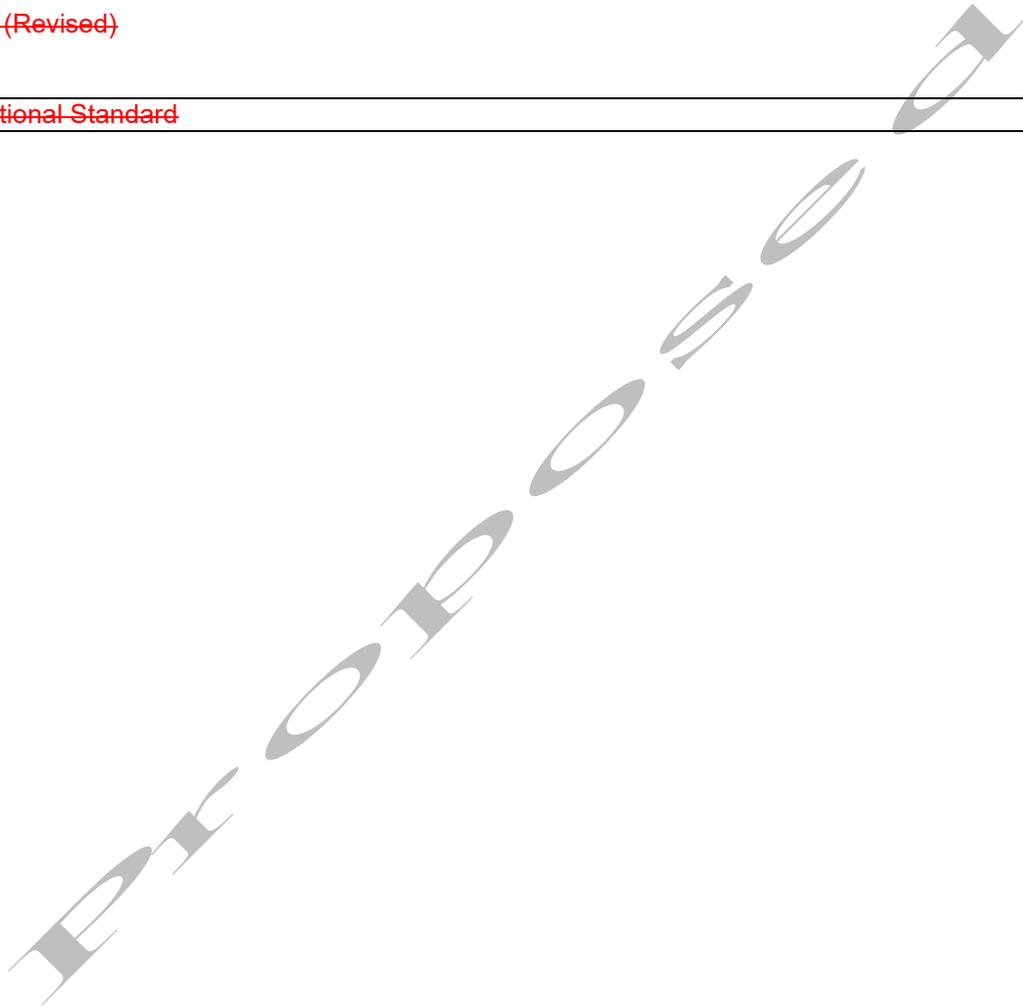
CONTENTS

	Paragraph
Introduction	
Scope of this ISA SAS	1
The Firm’s System of Quality Management and Role of Engagement Teams	2–9
Effective Date	10
Objective	11
Definitions	12
Requirements	
Leadership Responsibilities for Managing and Achieving Quality on Audits	13–15
Relevant Ethical Requirements, Including Those Related to Independence	16–21
Acceptance and Continuance of Client Relationships and Audit Engagements	22–24
Engagement Resources	25–28
Engagement Performance	29–38
Monitoring and Remediation	39
Taking Overall Responsibility for Managing and Achieving Quality	40
Documentation	41
Application and Other Explanatory Material	
Scope of this ISA SAS	A1
The Firm’s System of Quality Management and Role of Engagement Teams	A2–A14
Definitions	A15–A27
Leadership Responsibilities for Managing and Achieving Quality on Audits	A28–A37
Relevant Ethical Requirements, Including Those Related to Independence	A38–A48
Acceptance and Continuance of Client Relationships and Audit Engagements	A49–A58

Engagement Resources	A59–A79 <u>80</u>
Engagement Performance	A <u>80</u> 81–A408 <u>109</u>
Monitoring and Remediation	A409 <u>110</u> –A412 <u>113</u>
Taking Overall Responsibility for Managing and Achieving Quality	A413 <u>114</u> –A416 <u>117</u>
Documentation	A417 <u>118</u> –A420 <u>121</u>

ISA 220 (Revised)

International Standard



Statement on Auditing Standards Quality Management for an Audit of Financial Statements, should be read in conjunction with **ISA 200, Overall Objectives of the Independent Auditor and the Conduct of an Audit Engagement Conducted in Accordance With International Generally Accepted Auditing Standards** on Auditing.

<p>Introduction</p>	
<p>Scope of This ISA Statement on Auditing Standards</p>	
<p>1. This International Standard Statement on Auditing Standards (ISASAS) deals with addresses the specific responsibilities of the auditor regarding quality management at the engagement level for an audit of financial statements, and the related responsibilities of the engagement partner. This ISASAS also applies, adapted as necessary, to other engagements conducted in accordance with generally accepted auditing standards (GAAS) (for example, a review of interim financial information conducted in accordance with AU-C section 930, <i>Interim Financial Information</i>).[*] This SAS is to be read in conjunction with the AICPA Code of Professional Conduct (AICPA code) and other relevant ethical requirements. (Ref: par. A1, and A38)</p>	<p>Specific to ASB's jurisdiction.</p>
<p>2. Although government audit organizations are subject to the quality control and assurance requirements of <i>Government Auditing Standards</i>, and <i>Statements on Quality Management Standards (SQMSs)</i> are not applicable to auditors in government audit organizations,¹ this SAS is applicable to auditors in government audit organizations who perform financial audits in accordance with GAAS.</p>	<p>Specific to ASB's jurisdiction.</p>
<p>The Firm's System of Quality Management and the Role of Engagement Teams</p>	
<p>3. 2- Under ISQM 1 SQMS No. 1, <i>A Firm's System of Quality Management</i>, the objective of the firm is to design, implement, and operate a system of quality management for audits or reviews of financial statements, or other assurance or related services engagements performed by the firm, in its accounting and auditing practice that provides the firm with reasonable assurance that: (Ref: par. A132–A143)</p>	<p>Specific to ASB's jurisdiction.</p>
<p>a. the firm and its personnel fulfill their responsibilities in accordance with professional standards and applicable legal and regulatory requirements, and conduct engagements in accordance with such standards and requirements, and</p>	

* All AU-C sections can be found in *AICPA Professional Standards*.

¹ Paragraph 5 of *Statement on Quality Management Standards (SQMS) No. 1, A Firm's System of Quality Management*.

<p>b. engagement reports issued by the firm or engagement partners are appropriate in the circumstances.^{1 2}</p>	
<p>3. This ISA is premised on the basis that the firm is subject to the ISQMs or to national requirements that are at least as demanding. (Ref: Para. A2–A3)</p>	<p>Specific to ASB’s jurisdiction.</p>
<p>4. The engagement team, led by the engagement partner, is responsible, within the context of the firm’s system of quality management and through complying with the requirements of this ISA<u>SAS</u>, for <u>the following</u>: (Ref: par. A4–A11)</p>	<p>AICPA style</p>
<p>a. Implementing the firm’s responses to quality risks (i.e. that is, the firm’s policies or procedures) that are applicable to the audit engagement using information communicated by, or obtained from, the firm;</p>	<p>AICPA style</p>
<p>b. Given the nature and circumstances of the audit engagement, determining whether to design and implement responses at the engagement level beyond those in the firm’s policies or procedures; and</p>	
<p>c. Communicating to the firm information from the audit engagement that is required to be communicated by the firm’s policies or procedures <u>to be communicated</u> to support the design, implementation, and operation of the firm’s system of quality management</p>	<p>To clarify; no change in meaning intended</p>
<p>5. Complying with the requirements in other ISAs<u>AU-C sections</u> may provide information that is relevant to quality management at the engagement level. (Ref: par. A12)</p>	
<p>6. The public interest is served by the consistent performance of quality audit engagements through achieving, which are engagements that achieve the objective of this standard<u>SAS</u> and other ISAs for each engagement<u>AU-C sections</u>. A quality audit engagement is achieved through planning and performing the engagement and reporting on it in accordance with professional standards and applicable legal and regulatory requirements. Achieving the objectives of those standards and complying with the requirements of applicable law or regulation involves exercising professional judgment and exercising<u>maintaining</u> professional skepticism.</p>	<p>To clarify; no change in meaning intended ASB preferred wording</p>
<p>7. In accordance with ISA<u>AU-C section</u> 200, ²<u>Overall Objectives of the Independent Auditor and the Conduct of an Audit in Accordance With Generally</u></p>	

¹ ISQM 1, paragraph 14

² Paragraph 15 of SQMS No. 1.

<p><u>Accepted Auditing Standards</u>.³ the engagement team is required to plan and perform an audit with professional skepticism and to exercise professional judgment. Professional judgment is exercised in making informed decisions about the courses of action that are appropriate to manage and achieve quality given the nature and circumstances of the audit engagement. Professional skepticism supports the quality of judgments made by the engagement team and, through these judgments, supports the overall effectiveness of the engagement team in achieving quality at the engagement level. The appropriate exercise<u>maintenance</u> of professional skepticism may be demonstrated through the actions and communications of the engagement team. Such actions and communications may include specific steps to mitigate impediments that may impair the appropriate exercise<u>maintenance</u> of professional skepticism, such as unconscious bias or resource constraints. (Ref: par. A33–A36)</p>	
<p>Scalability</p>	
<p>8. The requirements of this ISA<u>SAS</u> are intended to be applied in the context of the nature and circumstances of each audit. For example<u>Examples</u> follow:</p>	<p>AICPA style</p>
<ul style="list-style-type: none"> • (a) When an audit is carried out entirely by the engagement partner, which may be the case for an audit of a less complex entity, some requirements in this ISA<u>SAS</u> are not relevant because they are conditional on the involvement of other members of the engagement team. (Ref: par. A13– A14) 	
<ul style="list-style-type: none"> • (b) When an audit is not carried out entirely by the engagement partner, or in an audit of an entity whose nature and circumstances are more complex, the engagement partner may assign the design or performance of some procedures, tasks, or actions to other members of the engagement team. 	
<p>The Engagement Partner’s Responsibilities</p>	
<p>9. The engagement partner remains ultimately responsible, and, therefore, accountable, for compliance with the requirements of this ISA<u>SAS</u>. The term “Nevertheless, the engagement partner shall<u>may seek assistance from others to fulfill these responsibilities. The phrase “take responsibility for…”</u> is used for those requirements that<u>for which</u> the engagement partner is permitted to assign the design or performance of procedures, tasks, or actions to appropriately skilled or suitably experienced members of the engagement team. For other requirements, this ISA<u>SAS</u> expressly intends that the requirement or responsibility be fulfilled by the engagement partner and, in such circumstances, the engagement partner may <u>need to</u> obtain information from</p>	<p>To clarify; no change in application intended</p>

²-ISA³ Paragraphs .17-.18 and .A22-.A31 of AU-C section 200, Overall Objectives of the Independent Auditor and the Conduct of an Audit in Accordance With ~~International~~Generally Accepted Auditing Standards ~~on Auditing, paragraphs 15-16 and A20-A24-~~

the firm or other members of the engagement team. <u>For example, when others perform supervisory and review responsibilities, the outcome of those activities can be taken into account by the engagement partner in fulfilling the requirement.</u> (Ref: par. A22–A25)	
Effective Date	
10. This ISA <u>SAS</u> is effective for audits of financial statements engagements conducted in accordance with GAAS for periods beginning on or after December 15, 2022 <u>2025</u> .	
Objective	
11. The objective of the auditor is to manage quality at the engagement level to obtain reasonable assurance that quality has been achieved such that:	
a. the auditor has fulfilled the auditor’s responsibilities, and has conducted the audit, in accordance with professional standards and applicable legal and regulatory requirements; and	
b. the auditor’s report issued is appropriate in the circumstances.	
Definitions	
12. For purposes of the ISAs <u>GAAS</u> , the following terms have the meanings attributed below <u>as follows</u> :	
(a) Engagement partner ³ – ⁴ The partner or other individual, appointed by the firm, who is responsible for the audit engagement and its performance, and for the auditor’s report that is issued on behalf of the firm, and who, where <u>when</u> required, has the appropriate authority from a professional, legal, or regulatory body.	Preferred wording
(b) Engagement quality review – ⁵ An objective evaluation of the significant judgments made by the engagement team and the conclusions reached thereon, performed by the engagement quality reviewer and completed on or before the date of the engagement report <u>is released</u> .	See paragraph 36d
(c) Engagement quality reviewer – ⁵ A partner, other individual in the firm, or an external individual, appointed by the firm to perform the engagement quality review.	
(d) Engagement team – ⁵ All partners and staff performing the audit engagement, and any other individuals who perform audit procedures on the engagement, excluding an auditor’s external expert ⁴ <u>specialist</u> ⁵ and internal	Preferred wording

³ “Engagement partner,” “partner,” and “firm” is to be read as referring to their public sector equivalents where relevant.

⁴ Engagement partner, partner, and firm refer to their governmental equivalents when relevant.

⁴ ISA ⁵ Paragraph .06 of AU-C section 620, *Using the Work of an Auditor’s Expert*, paragraph 6(a) Specialist, defines the term “auditor’s ~~expert~~specialist.”

<p>auditors who provide direct assistance on an engagement.⁵ (Ref: par. A15–A25)</p>	
<p>(e) Firm — A sole practitioner, partnership or corporation or other entity of professional accountants, or public sector equivalent. (Ref: Para. A26)</p> <p><u>Firm.</u> A form of organization permitted by law or regulation whose characteristics conform to resolutions of the Council of the AICPA and that is engaged in public practice. (Ref: par. A26)</p>	<p>To make specific to the U.S.</p>
<p><u>Inspection.</u> Inspection is an evaluation of the adequacy of aspects of the firm's quality management policies and procedures, its personnel's understanding of those policies and procedures, and the extent of the firm's compliance with them.</p>	<p>From extant QC sec. 10</p>
<p>(f) Network firm — A firm or entity that belongs to the firm's network. (Ref: Para. A27)</p>	<p>To make specific to the U.S.</p>
<p>(g) Network — A larger structure: (Ref: Para. A27)</p> <p>(i) That is aimed at cooperation, and</p> <p>(ii) That is clearly aimed at profit or cost-sharing or shares common ownership, control or management, common quality management policies or common business strategy, the use of a common brand name, or a significant part of professional resources</p>	
<p><u>Network.</u> As defined in "Definitions" (ET sec. 0.400)[‡] in the AICPA code, an association of entities that includes one or more firms (Ref: par. A27)</p>	
<p><u>Network firm.</u> As defined in "Definitions" (ET sec. 0.400) in the AICPA code, a firm or other entity that belongs to a network. References to a network firm are to be read hereafter as "another firm or entity that belongs to the same network as the firm." (Ref: par. A27)</p>	
<p>(h) Partner — Any individual with authority to bind the firm with respect to the performance of a professional services engagement. <u>For purposes of this definition, partner may include an employee with this authority who has not assumed the risks and benefits of ownership. Firms might use different titles to refer to individuals with this authority.</u></p>	<p>From extant QC sec. 10</p>
<p>(i) Personnel — Partners and staff in the firm.</p>	
<p>(j) Professional standards — International. <u>Standards promulgated by the AICPA Auditing (ISAs) Standards Board or the AICPA Accounting and Review Services Committee under the "General Standards Rule" (ET sec. 1.300.001) or the "Compliance With Standards Rule" (ET sec. 1.310.001) of the AICPA code, or by other standard-setting bodies that set auditing and attest standards</u></p>	<p>To make specific to the U.S.</p>

⁵ ISA⁶ AU-C section 610 (Revised 2013), *Using the Work of Internal Auditors*, establishes limits on the use of direct assistance. ~~It also acknowledges that the external auditor may be prohibited by law or regulation from obtaining direct assistance from internal auditors. Therefore, the use of direct assistance is restricted to situations where it is permitted.~~

[‡] All ET sections can be found in AICPA Professional Standards.

<p><u>applicable to the engagement being performed</u> and relevant ethical requirements.</p>	
<p>(k) Relevant ethical requirements—<u>Principles of professional ethics and ethical requirements that are applicable to professional accountants when undertaking to which the audit engagement. Relevant ethical requirements ordinarily comprise the provisions of the International Ethics Standards Board for Accountants’ International Code of Ethics for Professional Accountants (including International Independence Standards) (IESBA Code) related to audits of financial statements, together with national requirements, team and engagement quality reviewer are subject, which consist of the AICPA code together with rules of applicable state boards of accountancy and applicable regulatory agencies</u> that are more restrictive.</p>	<p>To make specific to the U.S.</p>
<p>(h) Response (in relation to a system of quality management)—<u>Policies or procedures designed and implemented by the firm to address one or more quality risk(s)risks:</u></p> <ul style="list-style-type: none"> • (i) Policies are statements of what should, or should not, be done to address a quality risk(s) <u>or risks</u>. Such statements may be documented, explicitly stated in communications, or implied through actions and decisions. • (ii) Procedures are actions to implement policies. 	<p>AICPA style</p>
<p>(m) Staff—<u>Professionals, other than partners, including any experts</u><u>specialist</u> the firm employs.</p>	<p>Preferred word</p>
<p>Requirements</p>	
<p>Leadership Responsibilities for Managing and Achieving Quality on Audits</p>	
<p>13. The engagement partner shall<u>should</u> take overall responsibility for managing and achieving quality on the audit engagement, including taking responsibility for creating an environment for the engagement that emphasizes the firm’s culture and expected behavior of engagement team members. In doing so, the engagement partner shall<u>should</u> be sufficiently and appropriately involved throughout the audit engagement such that the engagement partner has the basis for determining whether the significant judgments made, and the conclusions reached, are appropriate given the nature and circumstances of the engagement. (Ref: par. A28–A37)</p>	<p>ASB preferred word</p>
<p>14. In creating the environment described in paragraph 13, the engagement partner shall<u>should</u> take responsibility for clear, consistent, and effective actions being taken that reflect the firm’s commitment to quality and <u>that</u> establish and communicate the expected behavior of engagement team members, including emphasizing <u>the following</u>: (Ref: par. A30–A34)</p>	
<p>a. That all engagement team members are responsible for contributing to the management and achievement of quality at the engagement level;</p>	<p>AICPA style</p>

<p>b. The importance of professional ethics, values, and attitudes to the members of the engagement team;</p>	
<p>c. The importance of open and robust communication within the engagement team, and supporting the ability of engagement team members to raise concerns without fear of reprisal; and</p>	
<p>d. The importance of each engagement team member exercising maintaining professional skepticism throughout the audit engagement</p>	<p>ASB preferred work</p>
<p>15. If the engagement partner assigns the design or performance of procedures, tasks, or actions related to a requirement of this ISASAS to other members of the engagement team to assist the engagement partner in complying with the requirements of this ISASAS, the engagement partner shallshould continue to take overall responsibility for managing and achieving quality on the audit engagement through direction and supervision of those members of the engagement team, and review of their work. (Ref: par. 9, and A37)</p>	
<p>Relevant Ethical Requirements, Including Those Related to Independence</p>	
<p>16. The engagement partner shallshould have an understanding of the relevant ethical requirements, including those related to independence, that are applicable given the nature and circumstances of the audit engagement. (Ref: par. A38–A42, and A48)</p>	
<p>17. The engagement partner shallshould take responsibility for other members of the engagement team having been made aware of relevant ethical requirements that are applicable given the nature and circumstances of the audit engagement, and the firm’s related policies or procedures, including those that address <u>the following</u>: (Ref: par. A23–A25, and A40–A44)</p>	
<p>a. Identifying, evaluating, and addressing threats to compliance with relevant ethical requirements, including those related to independence;</p>	
<p>b. Circumstances that may cause a breach of relevant ethical requirements, including those related to independence, and the responsibilities of members of the engagement team when they become aware of breaches; and</p>	
<p>c. The responsibilities of members of the engagement team when they become aware of an instance of non-compliance with laws and regulations by the entity⁶ <u>Z</u></p>	

⁶ ISA 250 (Revised), *Consideration of Laws and Regulations in an Audit of Financial Statements*

⁷ See AU-C section 250, *Consideration of Laws and Regulations in an Audit of Financial Statements*.

<p>18. If matters come to the engagement partner’s attention that indicate that a threat to compliance with relevant ethical requirements exists, the engagement partner shall<u>should</u> evaluate the threat through threats by complying with the firm’s policies or procedures, using relevant information from the firm, the engagement team, or other sources, and take appropriate action. (Ref: par. A43–A44)</p>	<p>AICPA style</p>
<p>19. The engagement partner shall<u>should</u> remain alert throughout the audit engagement, through observation and making inquiries as necessary, for breaches of relevant ethical requirements or the firm’s related policies or procedures by members of the engagement team. (Ref: par. A45)</p>	
<p>20. If matters come to the engagement partner’s attention through the firm’s system of quality management, or from other sources, that indicate that relevant ethical requirements applicable to the nature and circumstances of the audit engagement have not been fulfilled, the engagement partner, in consultation with others in the firm, shall<u>should</u> take appropriate action. (Ref: par. A46)</p>	
<p>21. Prior to dating the auditor’s report, the engagement partner shall<u>should</u> take responsibility for determining whether relevant ethical requirements, including those related to independence, have been fulfilled. (Ref: par. A38 and A47)</p>	
<p>Acceptance and Continuance of Client Relationships and Audit Engagements</p>	
<p>22. The engagement partner shall<u>should</u> determine that the firm’s policies or procedures for the acceptance and continuance of client relationships and audit engagements have been followed, and that conclusions reached in this regard are appropriate. (Ref: par. A49–A52, A58)</p>	
<p>23. The engagement partner shall<u>should</u> take into account information obtained in the acceptance and continuance process in planning and performing the audit engagement in accordance with the ISAs<u>GAAS</u> and complying with the requirements of this ISAS<u>SAS</u>. (Ref: par. A53–A56)</p>	
<p>24. If the engagement team becomes aware of information that may have caused the firm to decline the audit engagement had that information been known by the firm prior to accepting or continuing the client relationship or specific engagement, the engagement partner shall<u>should</u> communicate that information promptly to the firm, so that the firm and the engagement partner can take the necessary action. (Ref: par. A57)</p>	
<p>Engagement Resources</p>	
<p>25. The engagement partner shall<u>should</u> determine that sufficient and appropriate resources to perform the engagement are assigned or made available to the engagement team in a timely manner, taking into account the nature and circumstances of the audit engagement, the firm’s policies or procedures, and any changes that may arise during the engagement. (Ref: par. A59–A70<u>71</u>, A73–A74–A75, and A79<u>80</u>)</p>	

<p>26. The engagement partner shall<u>should</u> determine that members of the engagement team, and any auditor's external experts<u>specialists</u> and internal auditors who provide direct assistance who are not part of the engagement team, collectively have the appropriate competence and capabilities, including sufficient time, to perform the audit engagement. (Ref: par. A62, and <u>A7172–A7475</u>)</p>	
<p>27. If, as a result of complying with the requirements in paragraphs 25 and 26, the engagement partner determines that resources assigned or made available are insufficient or inappropriate in the circumstances of the audit engagement, the engagement partner shall<u>should</u> take appropriate action, including communicating with appropriate individuals about the need to assign or make available additional or alternative resources to the engagement. (Ref: par. A7576–A7879)</p>	
<p>28. The engagement partner shall<u>should</u> take responsibility for using the resources assigned or made available to the engagement team appropriately, given the nature and circumstances of the audit engagement. (Ref: par. A63–A69)</p>	
<p>Engagement Performance</p>	
<p><i>Direction, Supervision, and Review</i></p>	
<p>29. The engagement partner shall<u>should</u> take responsibility for the direction and supervision of the members of the engagement team and the review of their work. (Ref: par. A8031)</p>	
<p>30. The engagement partner shall<u>should</u> determine that the nature, timing, and extent of direction, supervision, and review is:are (Ref: par. A8182–A89,90 and A9495–A9798)</p>	<p>AICPA style</p>
<p>a. planned^{7,8} and performed in accordance with the firm's policies or procedures, professional standards, and applicable legal and regulatory requirements; and</p>	
<p>b. responsive to the nature and circumstances of the audit engagement and the resources assigned or made available to the engagement team by the firm.</p>	
<p>31. The engagement partner shall<u>should</u> review audit documentation at appropriate points in time during the audit engagement, including audit documentation relating to: (Ref: par. A9091–A9394)</p>	
<p>a. significant matters;^{8,9}</p>	
<p>b. significant judgments, including those relating to difficult or contentious matters identified during the audit engagement, and the conclusions reached; and</p>	

⁷-ISA⁸ [Paragraph .11 of AU-C section 300, Planning an Audit of Financial Statements](#); ~~paragraph 11.~~

⁸-ISA⁹ [Paragraph .08 of AU-C section 230, Audit Documentation](#); ~~paragraph 8(c).~~

<p>c. other matters that, in the engagement partner’s professional judgment, are relevant to the engagement partner’s responsibilities.</p>	
<p>32. On or before the date of the auditor’s report, the engagement partner shall<u>should</u> determine, through review of audit documentation and discussion with the engagement team, that sufficient appropriate audit evidence has been obtained to support the conclusions reached and for the auditor’s report to be issued. (Ref: par. A90<u>91</u>–A94<u>95</u>)</p>	
<p>33. Prior to dating the auditor’s report, the engagement partner shall<u>should</u> review the financial statements and the auditor’s report, including, if applicable, the description of the key audit matters⁹<u>10</u> and related audit documentation, to determine that the report to be issued will be appropriate in the circumstances.⁴⁰<u>11</u></p>	
<p>34. The engagement partner shall<u>should</u> review, prior to their issuance, formal written communications to management, those charged with governance, or regulatory authorities. (Ref: par. A98<u>99</u>)</p>	
<p>Consultation</p>	
<p>35. The engagement partner shall<u>should do the following</u>: (Ref: par. A99<u>100</u>–A102<u>103</u>)</p>	
<p>a. Take responsibility for the engagement team undertaking consultation on:</p>	
<p>i. difficult or contentious matters and matters on which the firm’s policies or procedures require consultation; and</p>	
<p>ii. other matters that, in the engagement partner’s professional judgment, require consultation; and.</p>	
<p>b. Determine that members of the engagement team have undertaken appropriate consultation during the audit engagement, both within the engagement team, and between the engagement team and others at the appropriate level within or outside the firm; and.</p>	
<p>c. Determine that the nature and scope of, and conclusions resulting from, such consultations are agreed with the party consulted; and.</p>	
<p>d. Determine that conclusions agreed have been implemented.</p>	
<p>Engagement Quality Review</p>	
<p>36. For audit engagements for which an engagement quality review is required, the engagement partner shall<u>should</u> (Ref: par. A103<u>104</u>)</p>	

⁹ISA¹⁰ See AU-C section 701, *Communicating Key Audit Matters in the Independent Auditor’s Report*.

⁴⁰ISA¹¹ See AU-C section 700 (Revised), *Forming an Opinion and Reporting on Financial Statements*, or ISA AU-C section 705 (Revised), *Modifications to the Opinion in the Independent Auditor’s Report*.

<p>a. determine that an engagement quality reviewer has been appointed;_±</p>	
<p>b. cooperate with the engagement quality reviewer and inform other members of the engagement team of their responsibility to do so;_±</p>	
<p>c. discuss significant matters and significant judgments arising during the audit engagement, including those identified during the engagement quality review, with the engagement quality reviewer; and_±</p>	
<p>d. not date<u>release</u> the auditor's report until the completion of the engagement quality review. (Ref: par. A104<u>105</u>–A106<u>107</u>)</p>	<p>The ASB believes that the flexibility of using the report release date provides greater benefit than the logistical cost of restricting the time available for completing the engagement quality review.</p>
<p>Differences of Opinion</p>	
<p>37. If differences of opinion arise within the engagement team, or between the engagement team and the engagement quality reviewer or individuals performing activities within the firm's system of quality management, including those who provide consultation, the engagement team shall<u>should</u> follow the firm's policies or procedures for dealing with and resolving such differences of opinion. (Ref: par. A107–A108–A109)</p>	
<p>38. The engagement partner shall<u>should</u></p>	
<p>a. take responsibility for differences of opinion being addressed and resolved in accordance with the firm's policies or procedures;_±</p>	
<p>b. determine that conclusions reached are documented and implemented;and_±</p>	
<p>c. not date the auditor's report until any differences of opinion are resolved.</p>	
<p>Monitoring and Remediation</p>	
<p>39. The engagement partner shall<u>should</u> take responsibility for <u>the following</u>: (Ref: par. A109<u>110</u>–A112<u>113</u>)</p>	
<p>a. Obtaining an understanding of the information from the firm's monitoring and remediation process, as communicated by the firm_± including, as applicable, the information from the monitoring and remediation process of the network and across the network firms;</p>	

<p>b. Determining the relevance and effect on the audit engagement of the information referred to in paragraph 39(a) and take<u>taking</u> appropriate action;and</p>	<p>AICPA style</p>
<p>c. Remaining alert throughout the audit engagement for information that may be relevant to the firm’s monitoring and remediation process and communicate<u>communicating</u> such information to those responsible for the process.</p>	
<p>Taking Overall Responsibility for Managing and Achieving Quality</p>	
<p>40. Prior to dating the auditor’s report, the engagement partner shall<u>should</u> determine that the engagement partner has taken overall responsibility for managing and achieving quality on the audit engagement. In doing so, the engagement partner shall<u>should</u> determine that: (Ref: par. A113<u>114</u>–A116<u>117</u>)</p>	
<p>a. the engagement partner’s involvement has been sufficient and appropriate throughout the audit engagement such that the engagement partner has the<u>an appropriate</u> basis for determining that the significant judgments made and the conclusions reached are appropriate given the nature and circumstances of the engagement;and.</p>	<p>To clarify; no change in application intended.</p>
<p>b. the nature and circumstances of the audit engagement, any changes thereto, and the firm’s related policies or procedures have been taken into account in complying with the requirements of this ISAS<u>SAS</u>.</p>	
<p>Documentation</p>	
<p>41. In applying ISA<u>AU-C section</u> 230,¹⁴ <u>Audit Documentation</u>, the auditor shall<u>should</u> include <u>the following</u> in the audit documentation:¹² (Ref: par. A117<u>118</u>–A120<u>121</u>)</p>	
<p>a. Matters<u>Significant issues</u> identified, relevant discussions with personnel, and conclusions reached with respect to:</p>	<p>To be consistent with other AU-C sections</p>
<p>i. fulfillment of responsibilities relating to relevant ethical requirements, including those related to independence.</p>	
<p>ii. the acceptance and continuance of the client relationship and audit engagement.</p>	
<p>b. The nature and scope of, and conclusions resulting from, consultations undertaken during the audit engagement and how such conclusions were implemented.</p>	

¹⁴ISA-230, paragraphs 8–11 and A6

¹² Paragraphs .08–.11 of AU-C section 230.

<p>c. If the audit engagement is subject to an engagement quality review, that the engagement quality review has been completed on or before the date<u>release</u> of the auditor's report.</p>	
<p style="text-align: center;">_____ * * *</p>	
<p>Application and Other Explanatory Material</p>	
<p>Scope of This ISA<u>SAS</u> (Ref: par. 1)</p>	
<p>A1. This ISA<u>SAS</u> applies to all audits of financial statements, including audits of group financial statements. ISA<u>AU-C section 600</u>¹². <u>Special Considerations — Audits of Group Financial Statements (Including the Work of Component Auditors)</u>, deals with special considerations that apply to an audit of group financial statements and, including when component auditors are involved. ISA<u>AU-C section 600 also provides guidance on how to adapt and apply the requirements of this SAS in an audit of group financial statements involving component auditors.</u> <u>AU-C section 600</u>, adapted as necessary in the circumstances, may also be useful in an audit of financial statements when the engagement team includes individuals from another firm. For example, ISA<u>AU-C section 600</u> may be useful when involving such an individual to attend a physical inventory count; inspect property, plant, and equipment; or perform audit procedures at a shared service center at a remote location.</p>	<p>Additional application material</p>
<p>The Firm's System of Quality Management and <u>the</u> Role of Engagement Teams (Ref: par. 23<u>9</u>)</p>	
<p>A2. ISQM<u>SQMS No. 1</u> deals with<u>addresses</u> a firm's responsibilities for designing, implementing, and operating its system of quality management.</p>	
<p>A3. Firms or national requirements may use different terminology or frameworks to describe the components of the system of quality management. National requirements that deal with the firm's responsibilities to design, implement and operate a system of quality management are at least as demanding as ISQM 1 when they address the requirements of ISQM 1 and impose obligations on the firm to achieve the objective of ISQM 1.</p>	<p>Specific to U.S.</p>
<p>The Engagement Team's Responsibilities Relating to the Firm's System of Quality Management (Ref: par. 4)</p>	
<p>A4. Quality management at the engagement level is supported by the firm's system of quality management and informed by the specific nature and circumstances of the audit engagement. In accordance with ISQM<u>SQMS No. 1</u>, the firm is responsible for communicating information <u>that</u> enables the engagement team to understand and carry out their responsibilities relating to performing engagements. For example, such communications may cover policies or procedures to undertake consultations with designated individuals in certain situations involving complex technical or ethical matters, or to involve</p>	<p>AICPA style</p>

¹² ISA 600, *Special Considerations—Audits of Group Financial Statements (Including the Work of Component Auditors)*

<p>firm-designated experts in specific engagements to perform audit procedures related to particular matters (e.g. for example, the firm may specify that firm-designated credit-<u>risk modeling</u> experts are to be involved in auditing expected credit loss allowances in audits of financial institutions).</p>	
<p>A5. Firm-level responses may include policies or procedures established by a network; or by other firms, structures, or organizations within the same network (network requirements or network services are described further in <u>ISQMSQMS No. 1</u> within the “Network Requirements or Network Services” section).¹³ <u>13</u> The requirements of this <u>ISASAS</u> are based on the premise that the firm is responsible for taking the necessary action to enable engagement teams to implement or use network requirements or network services on the audit engagement (for example, a requirement to use an audit methodology developed for use by a network firm). Under <u>ISQMSQMS No. 1</u>, the firm is responsible for determining how network requirements or network services are relevant to, and are taken into account in, the firm’s system of quality management.¹⁴ <u>14</u></p>	
<p>A6. Some firm-level responses to quality risks are not performed at the engagement level but are, nevertheless, relevant when complying with the requirements of this <u>ISASAS</u>. For example, firm-level responses that the engagement team may be able to depend on when complying with the requirements of this <u>ISASAS</u> include <u>the following</u>:</p>	
<ul style="list-style-type: none"> • Personnel recruitment and professional training processes; 	
<ul style="list-style-type: none"> • The information technology (IT) applications that support the firm’s monitoring of independence; 	
<ul style="list-style-type: none"> • The development of IT applications that support the acceptance and continuance of client relationships and audit engagements; and 	
<ul style="list-style-type: none"> • The development of audit methodologies and related implementation tools and guidance. 	
<p>A7. Due to the specific nature and circumstances of each audit engagement and changes that may occur during the audit engagement, a firm cannot identify all quality risks that may arise at the engagement level or set forth all relevant and appropriate responses. Accordingly, the engagement team exercises professional judgment in determining whether to design and implement responses, beyond those set forth in the firm’s policies or procedures, at the engagement level to meet the objective of this <u>ISASAS</u>.¹⁵ <u>15</u></p>	

¹³ ISQM 1, paragraph 49(b)

¹³ Paragraph 50b of SQMS No. 1.

¹⁴ ISQM 1, paragraph 49(a)

¹⁴ Paragraph 50a of SQMS No. 1.

¹⁵ ISA¹⁵ AU-C section 200 requires the auditor to exercise professional judgment in planning and performing an audit of financial statements.

<p>A8. The engagement team's determination of whether engagement <u>level</u> responses are necessary (and, if so, what those responses are) is influenced by the requirements of this ISASAS, the engagement team's understanding of the nature and circumstances of the engagement, and any changes during the audit engagement. For example, unanticipated circumstances may arise during the engagement that may cause the engagement partner to request the involvement of appropriately experienced personnel in addition to those initially assigned or made available <u>by the firm</u>.</p>	<p>To clarify; no change in application intended</p>
<p>A9. The relative balance of the engagement team's efforts to comply with the requirements of this ISASAS (i.e. that is, between implementing the firm's responses and designing and implementing engagement <u>specific</u> responses beyond those set forth in the firm's policies or procedures) may vary. For example, the firm may design an audit program to be used in circumstances that are applicable to the audit engagement (e.g. for example, an industry-specific audit program). Other than determining the timing and extent of procedures to be performed, there may be little or no need for supplemental audit procedures to be added to the audit program at the engagement level. Alternatively, the engagement team's actions in complying with the engagement performance requirements of this ISASAS may be more focused on designing and implementing responses at the engagement level to deal with the specific nature and circumstances of the engagement (e.g. for example, planning and performing procedures to address risks of material misstatement not contemplated by the firm's audit programs).</p>	
<p>A10. Ordinarily, the engagement team may depend on the firm's policies or procedures in complying with the requirements of this ISASAS, unless:</p>	
<ul style="list-style-type: none"> the engagement team's understanding or practical experience indicates that the firm's policies or procedures will not effectively address the nature and circumstances of the engagement; or 	
<ul style="list-style-type: none"> information provided by the firm or other parties, about the effectiveness of such policies or procedures suggests otherwise (e.g. they cannot be relied on (for example, information provided by the firm's monitoring activities, external inspections, or other relevant sources, indicates that the firm's policies or procedures are not operating effectively). 	<p>To clarify; no change in application intended</p>
<p>A11. If the engagement partner becomes aware (including through<u>by</u> being informed by other members of the engagement team) that the firm's responses to quality risks are ineffective in the context of the specific engagement, or the engagement partner is unable to depend on the firm's policies or procedures, the engagement partner communicates such information promptly to the firm in accordance with paragraph 39c as <u>because</u> such information is relevant to the firm's monitoring and remediation process. For example, if an engagement team member identifies that an audit software program has a security weakness, timely communication of such information to the appropriate personnel enables</p>	<p>AICPA style</p>

<p>the firm to take steps to update and reissue the audit program. See also paragraph A7069 in respect of sufficient and appropriate resources.</p>	
<p>Information Relevant to Quality Management at the Engagement Level (Ref: par. 65)</p>	
<p>A12. Complying with the requirements in other ISAsAU-C sections may provide information that is relevant to quality management at the engagement level. For example, the understanding of the entity and its environment required to be obtained under ISAAU-C section 315 (Revised 2019)¹⁶. <u>Understanding the Entity and Its Environment and Assessing the Risks of Material Misstatement</u>, provides information that may be relevant to complying with the requirements of this ISASAS. Such information may be relevant to the determination of <u>one or more of the following</u>:</p>	
<ul style="list-style-type: none"> • The nature of resources to deploy for specific audit areas, such as the use of appropriately experienced team members for high-risk areas; or the involvement of experts to deal with complex matters; 	
<ul style="list-style-type: none"> • The amount of resources to allocate to specific audit areas, such as the number of team members assigned to attend the physical inventory count at multiple locations; 	
<ul style="list-style-type: none"> • The nature, timing, and extent of review of the work performed by members of the team based on the assessed risks of material misstatement; or 	
<ul style="list-style-type: none"> • The allocation of the budgeted audit hours, including allocating more time, and the time of more experienced engagement team members to those areas where there are more risks of material misstatement or the identified risks are assessed as higher. 	
<p>Scalability (Ref: par. 2, 8)</p>	
<p>A13. In a smaller firm, the firm's policies or procedures may designate an engagement partner <u>or partners</u>, on behalf of the firm, to design many of the responses to the firm's quality risks as because doing so may be a more effective approach to designing and implementing responses as part of the firm's system of quality management. Additionally, a smaller firm's policies or procedures may be less formal. For example, in a very small firm with a relatively small number of audit engagements, the firm may determine that there is no need to establish a firm-wide system to monitor independence, and, rather, independence will be monitored at the individual engagement level by the engagement partner.</p>	
<p>A14. The requirements relating to direction, supervision, and review of the work of other members of the engagement team are only relevant if there are members of the engagement team other than the engagement partner.</p>	

¹⁶ ISA 315 (Revised 2019), *Identifying and Assessing the Risks of Material Misstatement*

Definitions	
Engagement Team (Ref: par. 12(d))	
A15. The engagement team may be organized in a variety of ways. For example, engagement team members may be located together or across different geographic locations and may be organized in groups by the activity they are performing. Regardless of how the engagement team is organized, any individual who performs audit procedures ¹⁷ ¹⁶ on the audit engagement, <u>excluding an auditor's external specialist¹⁷ and internal auditors who provide direct assistance on an engagement,¹⁸</u> is a member of the engagement team.	To clarify; no change in application intended
A16. The definition of an <i>engagement team</i> focuses on individuals who perform audit procedures on the audit engagement. <i>Audit evidence</i> , which is necessary to support the auditor's opinion and report, is primarily obtained from audit procedures performed during the course of the audit. ¹⁸ ¹⁹ Audit procedures comprise risk assessment procedures ¹⁹ ²⁰ and further audit procedures. ²⁰ ²¹ As explained in <u>ISA AU-C section 500, <i>Audit Evidence</i></u> , audit procedures include inspection, observation, confirmation, recalculation, reperformance, analytical procedures, and inquiry, often performed in some combination. ²⁴ ²² Other <u>ISAs AU-C sections</u> may also include specific procedures to obtain audit evidence, for example, <u>ISA AU-C section 520, <i>Analytical Procedures</i></u> . ²²	
A17. Engagement teams include personnel and may also include other individuals who perform audit procedures who are from:	
<ul style="list-style-type: none"> • (a) a network firm; or, • (b) a firm that is not a network firm, or • another service provider.²³²³ 	To clarify; no change in application intended
For example, an individual from another firm may perform audit procedures on the financial information of a component in a group audit engagement, attend a physical inventory count, or inspect physical fixed assets at a remote location.	

¹⁷ ISA 500, *Audit Evidence*, paragraph A10

¹⁶ Paragraph .A44 of AU-C section 500, *Audit Evidence*.

¹⁷ Paragraph .06 of AU-C section 620 defines the term *auditor's specialist*.

¹⁸ AU-C section 610 establishes limits on the use of direct assistance.

¹⁸ ISA 200,¹⁹ Paragraph .A30-32 of AU-C section 200.

¹⁹ ISA²⁰ AU-C section 315 (Revised 2019), *Understanding the Entity and Its Environment and Assessing the Risks of Material Misstatement*, provides requirements related to risk assessment procedures.

²⁰ ISA²¹ AU-C section 330, *The Auditor's Responses Performing Audit Procedures in Response to Assessed Risks and Evaluating the Audit Evidence Obtained*, provides requirements related to further audit procedures, including tests of controls and substantive procedures.

²⁴ ISA 500, paragraphs A14–A25²² Paragraph .A43 of AU-C section 500.

²² ISA 520, *Analytical Procedures*

²³ ISQM 1,²³ Paragraph 16(v) 17v of proposed SQMS No. 1.

<p>A18. Engagement teams may also include individuals from service delivery centers who perform audit procedures. For example, it may be determined that specific tasks that are repetitive or specialized in nature will be performed by a group of appropriately skilled personnel and, thus, the engagement team therefore includes such individuals. Service delivery centers may be established by the firm, the network, or by other firms, structures, or organizations within the same network. For example, a centralized function may be used to facilitate external confirmation procedures.</p>	<p>AICPA style</p>
<p>A19. Engagement teams may include individuals with expertise in a specialized area of accounting or auditing who perform audit procedures on the audit engagement, for example, individuals with expertise in accounting for income taxes, or in analyzing complex information produced by automated tools and techniques for the purpose of identifying unusual or unexpected relationships. An individual is not a member of the engagement team if that individual's involvement with the engagement is limited to consultation. Consultations are addressed in paragraphs 35 and A99–A102.</p>	
<p>A20. If the audit engagement is subject to an engagement quality review, the engagement quality reviewer, and any other individuals performing the engagement quality review, are not members of the engagement team. Such individuals may be subject to specific independence requirements.</p>	
<p>A21. An internal auditor providing direct assistance and an auditor's external expert <u>specialist</u> whose work is used in the engagement are not members of the engagement team.²⁴ ISA 610 (Revised) 2013 <u>AU-C section 610, Using the Work of Internal Auditors,</u> and ISA section 620, Using the Work of an Auditor's Specialist, provide requirements and guidance for the auditor when using the work of internal auditors in a direct assistance capacity or when using the work of an external expert <u>specialist</u>, respectively. Compliance with these ISAs <u>AU-C sections</u> requires the auditor to obtain sufficient appropriate audit evidence on the work performed by an internal auditor <u>who is</u> providing direct assistance and <u>to</u> perform audit procedures on the work of an auditor's expert <u>specialist</u>.</p>	<p>ASB preferred wording</p>
<p><i>The Engagement Partner's Responsibilities (Ref: par. 9, 12(d))</i></p>	
<p>A22. When this ISA <u>SAS</u> expressly intends that a requirement or responsibility be fulfilled by the engagement partner, the engagement partner may need to obtain information from the firm or other members of the engagement team to fulfill <u>fulfill</u> the requirement (e.g. for example, information to make the required decision or judgment). For example, the engagement partner is required to determine that members of the engagement team collectively have the appropriate competence and capabilities to perform the audit engagement. To make a judgment on whether the competence and capabilities of the engagement team is <u>are</u> appropriate, the engagement partner may need to use information compiled by the engagement team or from the firm's system of quality management.</p>	

²⁴ See ISA 620, paragraphs 12–13 and ISA 610 (Revised 2013), paragraphs 21–25.

²⁴ See paragraphs .12–.13 of AU-C section 620 and paragraphs .20–.24 of AU-C section 610.

<p>The Application of Firm Policies or Procedures by Members of the Engagement Team (Ref: par. 9,12(d),8 and par. 17)</p>	
<p>A23. Within the context of the firm’s system of quality management, engagement team members from the firm are responsible for implementing the firm’s policies or procedures that are applicable to the audit engagement. As Engagement team members from another firm are neither partners nor staff of the engagement partner’s firm. As such, they may not be subject to the firm’s system of quality management or the firm’s policies or procedures. Further, the policies or procedures of another firm may not be similar to that those of the engagement partner’s firm. For example, policies or procedures regarding direction, supervision, and review may be different, particularly when the other firm is in a jurisdiction with a different legal system, language, or culture than that of the engagement partner’s firm. Accordingly, if when the engagement team includes individuals who are from another firm, different actions may need to be taken by the firm or the engagement partner to implement the firm’s policies or procedures in with respect of to the work of those individuals.</p>	<p>AICPA preferred wording</p>
<p>A24. In particular, the firm’s policies or procedures may require the firm or the engagement partner to take different actions from those applicable to personnel when obtaining an understanding of whether an individual from another firm:</p>	
<ul style="list-style-type: none"> has the appropriate competence and capabilities to perform the audit engagement. For example, the individual would not be subject to the firm’s recruitment and training processes, and therefore, the firm’s policies or procedures may state that this determination can be made through other actions such as obtaining information from the other firm or a licensing or registration oversight body. Paragraphs 1922 and A3847–A48 of ISA <u>IAU-C section 600</u> contain guidance on obtaining an understanding of the competence and capabilities of component auditors. 	<p>Specific to U.S.</p>
<ul style="list-style-type: none"> understands the ethical requirements that are relevant to the group audit engagement. For example, the individual would not be subject to the firm’s training in respect of <u>with regard to</u> the firm’s policies or procedures for relevant ethical requirements. The firm’s policies or procedures may state that this understanding is obtained through other actions such as providing information, manuals, or guides containing the provisions of the relevant ethical requirements applicable to the audit engagement to the individual. 	<p>ASB preferred wording</p>
<ul style="list-style-type: none"> will confirm independence. For example, individuals who are not personnel may not be able to complete independence declarations directly on the firm’s independence systems. The firm’s policies or procedures may state that such individuals can provide evidence of their independence in relation to the audit engagement in other ways, such as <u>through</u> written confirmation. 	
<p>A25. When firm policies or procedures require specific activities to be undertaken in certain circumstances (e.g. for example, consultation on a particular matter), it may be necessary for the firm’s related policies or procedures to be communicated to <u>to communicate with</u> individuals who are not personnel. Such individuals are then able to alert the engagement partner if the circumstance arises, and this enables <u>about what is expected of them to enable</u></p>	<p>To clarify; no change in application intended</p>

<p>the engagement partner to comply with the firm’s policies or procedures. For example, in a group audit engagement, if a component communicating the group auditor is performing audit’s policies and procedures on the financial information of a <u>about matters subject to consultation to a component auditor enables the component and identifies a</u> <u>auditor to determine which identified</u> difficult or contentious matter <u>matters</u> that is <u>are</u> relevant to the group financial statements and subject to consultation²⁵ under the group auditor’s policies or procedures, <u>the component auditor is able to alert</u> <u>to bring to the attention of</u> the group engagement team about the matter.</p>	
<p>Firm (Ref: par. 12(e))</p>	
<p>A26. The definition of <i>firm</i> in relevant ethical requirements may differ from the definition set out in this ISASAS.</p>	
<p>“Network” and “Network Firm” (Ref: par. 12(f)–12(g))</p>	
<p>A27. The definitions of “<i>network</i>” or “<i>network firm</i>” in relevant ethical requirements may differ from those set out in this ISASAS. The IESBA <u>AICPA</u> code also provides guidance in relation to the terms “<i>network</i>” and “<i>network firm</i>.” Networks and the other network firms may be structured in a variety of ways, and are in all cases external to the firm. The provisions in this ISASAS in relation to networks also apply to any structures or organizations that do not form part of the firm, but that exist within the network.</p>	
<p>Leadership Responsibilities for Managing and Achieving Quality on <u>in</u> Audits (Ref: par. 13–15)</p>	
<p><i>Taking Overall Responsibility for Managing and Achieving Quality</i></p>	
<p>A28. ISQM SQMS No. 1 requires the firm to establish quality objectives that address the firm’s governance and leadership that supports, which support the design, implementation, and operation of the system of quality management. The engagement partner’s responsibility for managing and achieving quality is supported by a firm culture that demonstrates a commitment to quality. In addressing the requirements in paragraphs 13 and 14 of this ISASAS, the engagement partner may communicate directly to other members of the engagement team and reinforce this communication through personal conduct and actions (e.g., such as leading by example). A culture that demonstrates a commitment to quality is further shaped and reinforced by the engagement team members as they demonstrate expected behaviors when performing the engagement.</p>	<p>AICPA style</p>
<p><i>Scalability</i></p>	
<p>A29. The nature and extent of the actions of the engagement partner to demonstrate the firm’s commitment to quality may depend on a variety of factors, including the size, structure, geographical dispersion, and complexity of the firm and the engagement team, and the nature and circumstances of the audit engagement. With a smaller engagement team with few engagement team members, influencing the desired culture through direct interaction and conduct</p>	

²⁵ See paragraph 35.

may be sufficient, whereas for a larger engagement team that is dispersed over many locations, more formal communications may be necessary.	
Sufficient and Appropriate Involvement	
A30. Being sufficiently and appropriately involved throughout the audit engagement may be demonstrated by the engagement partner in different ways, including <u>the following</u> :	
<ul style="list-style-type: none"> • Taking responsibility for the nature, timing₂ and extent of the direction and supervision of the members of the engagement team₇ and the review of their work in complying with the requirements of this ISA₂₆ and SAS₂₅ 	
<ul style="list-style-type: none"> • Varying the nature, timing₂ and extent of such direction, supervision₂ and review in the context of the nature and circumstances of the engagement₂. 	
Communication	
A31. Communication is the means through which the engagement team shares relevant information on a timely basis to comply with the requirements of this ISA ₂₆ SAS ₂₅ , thereby contributing to the achievement of quality on the audit engagement. Communication may be between or among members of the engagement team ₇ or with ₂ :	
<ul style="list-style-type: none"> a. the firm₇ (e-g-for example₂₆, individuals performing activities within the firm's system of quality management, including those assigned ultimate or operational responsibility for the firm's system of quality management)₂; 	
<ul style="list-style-type: none"> b. others involved in the audit (e-g-for example₂₆, internal auditors who provide direct assistance²⁶ ₂₅ or an auditor's external expert²⁷); and specialist²⁶), or 	
<ul style="list-style-type: none"> c. parties that are external to the firm (e-g-for example₂₆, management, those charged with governance₂ or regulatory authorities). 	
A32. The nature and circumstances of the audit engagement may affect the engagement partner's decisions regarding the appropriate means of effective communication with the members of the engagement team. For example, to support appropriate direction, supervision ₂ and review, the firm may use IT applications to facilitate the communication between the members of the engagement team when they are performing work across different geographical locations.	

²⁶ See ISA 610 (Revised 2013), paragraph A41.

²⁵ See paragraph .A47 of AU-C section 610.

²⁷ See ISA 620, paragraphs 11(c) and A30.

²⁶ See paragraphs .11c and .A33 of AU-C section 620.

<p>Professional Skepticism (Ref: par. 7)</p>	
<p>A33. The engagement partner is responsible for emphasizing the importance of each engagement team member exercising<u>maintaining</u> professional skepticism throughout the audit engagement. Conditions inherent in some audit engagements can create pressures on the engagement team that may impede the appropriate exercise of professional skepticism when designing and performing audit procedures and evaluating audit evidence. Accordingly, when developing the overall audit strategy in accordance with ISA<u>IAU-C section 300, Planning an Audit</u>, the engagement team may need to consider whether such conditions exist in the audit engagement and, if so, what actions the firm or the engagement team may need to undertake to mitigate such impediments.</p>	
<p>A34. Impediments to the exercise of professional skepticism at the engagement level may include, but are not limited to <u>the following</u>:</p>	
<ul style="list-style-type: none"> • Budget constraints, which may discourage the use of sufficiently experienced or technically qualified resources, including experts, necessary for audits of entities wherein <u>which</u> technical expertise or specialized skills are needed for effective understanding, assessment of, and responses to risks and informed questioning of management. 	
<ul style="list-style-type: none"> • Tight deadlines, which may negatively affect the behavior of those who perform the work as well as those who direct, supervise, and review. For example, external time pressures may create restrictions to analyzing complex information effectively. 	
<ul style="list-style-type: none"> • Lack of cooperation or undue pressures imposed by management, which may negatively affect the engagement team’s ability to resolve complex or contentious issues. 	
<ul style="list-style-type: none"> • Insufficient understanding of the entity and its environment, its system of internal control, and the applicable financial reporting framework, which may constrain the ability of the engagement team to make appropriate judgments and an informed questioning of management’s assertions. 	
<ul style="list-style-type: none"> • Difficulties in obtaining access to records, facilities, certain employees, customers, vendors, or others, which may cause the engagement team to bias the selection of sources of audit evidence and seek audit evidence from sources that are more easily accessible. 	
<ul style="list-style-type: none"> • Overreliance on automated tools and techniques, which may result in the engagement team not critically assessing audit evidence. 	
<p>A35. Unconscious or conscious auditor biases may affect the engagement team’s professional judgments, including, for example, in the design and performance of audit procedures, or the evaluation of audit evidence. Examples of unconscious auditor biases that may impede the exercise of professional</p>	

<p>skepticism, and therefore, the reasonableness of the professional judgments made by the engagement team in complying with the requirements of this ISA, SAS may include the following:</p>	
<ul style="list-style-type: none"> • <i>Availability bias</i>, which is a tendency to place more weight on events or experiences that immediately come to mind or are readily available than on those that are not. 	
<ul style="list-style-type: none"> • <i>Confirmation bias</i>, which is a tendency to place more weight on information that corroborates an existing belief than information that contradicts or casts doubt on that belief. 	
<ul style="list-style-type: none"> • <i>Groupthink</i>, which is a tendency to think or make decisions as a group that discourages, <u>discouraging</u> creativity or individual responsibility. 	<p>To clarify; no change in application intended</p>
<ul style="list-style-type: none"> • <i>Overconfidence bias</i>, which is a tendency to overestimate one's own ability to make accurate assessments of risk or other judgments or decisions. 	
<ul style="list-style-type: none"> • <i>Anchoring bias</i>, which is a tendency to use an initial piece of information as an anchor against which subsequent information is inadequately assessed. 	
<ul style="list-style-type: none"> • <i>Automation bias</i>, which is a tendency to favor output generated from automated systems, even when human reasoning or contradictory information raises questions as to <u>about</u> whether such output is reliable or fit for purpose. 	
<p>A36. Possible actions that the engagement team may take to mitigate impediments to the exercise of professional skepticism at the engagement level may include the following:</p>	
<ul style="list-style-type: none"> • Remaining alert to changes in the nature or circumstances of the audit engagement that necessitate additional or different resources for the engagement, and requesting additional or different resources from those individuals within the firm responsible for allocating or assigning resources to the engagement. 	
<ul style="list-style-type: none"> • Explicitly alerting the engagement team to instances or situations <u>when in which</u> vulnerability to unconscious or conscious auditor biases may be greater (e.g. for example, areas involving greater judgment) and emphasizing the importance of seeking advice from more experienced members of the engagement team in planning and performing audit procedures. 	
<ul style="list-style-type: none"> • Changing the composition of the engagement team, for example, requesting that more experienced individuals with greater skills or knowledge or specific expertise are <u>be</u> assigned to the engagement. 	

<ul style="list-style-type: none"> Involving more experienced members of the engagement team when dealing with members of management who are difficult or challenging to interact with. 	
<ul style="list-style-type: none"> Involving members of the engagement team with specialized skills and knowledge or an auditor's expert to assist the engagement team with complex or subjective areas of the audit. 	
<ul style="list-style-type: none"> Modifying the nature, timing, and extent of direction, supervision, or review by involving more experienced engagement team members, more in-person oversight on a more frequent basis, or more in-depth reviews of certain working papers for: <ul style="list-style-type: none"> complex or subjective areas of the audit; areas that pose risks to achieving quality on the audit engagement; areas with a fraud risk; and identified or suspected non-compliance with laws or regulations. 	
<ul style="list-style-type: none"> Setting expectations for: <ul style="list-style-type: none"> less experienced members of the engagement team to seek advice frequently and in a timely manner from more experienced engagement team members or the engagement partner; and more experienced members of the engagement team to be available to less experienced members of the engagement team throughout the audit engagement and to respond positively and in a timely manner to their insights, requests for advice, or assistance. 	
<ul style="list-style-type: none"> Communicating with those charged with governance when management imposes undue pressure or the engagement team experiences difficulties in obtaining access to records, facilities, certain employees, customers, vendors, or others from whom audit evidence may be sought. 	
<p>Assigning Procedures, Tasks, or Actions to Other Members of the Engagement Team (Ref: par. 15)</p>	
<p>A37. Being sufficiently and appropriately involved throughout the audit engagement when procedures, tasks, or actions have been assigned to other members of the engagement team may be demonstrated by the engagement partner in different ways, including the following:</p>	
<ul style="list-style-type: none"> Informing assignees about the nature of their responsibilities and authority, the scope of the work being assigned and the objectives 	

thereof, and to provide any other necessary instructions and relevant information.	
<ul style="list-style-type: none"> • Direction <u>Directing</u> and supervision of <u>supervising</u> the assignees. 	
<ul style="list-style-type: none"> • Review of <u>Reviewing</u> the assignees' work to evaluate the conclusions reached, in addition to the requirements in paragraphs 29–34. 	
Relevant Ethical Requirements, Including Those Related to Independence (Ref: par. 16–21)	
Relevant Ethical Requirements (Ref: par. 1, 16–21)	
<p>A38. ISA AU-C section 200 ²⁸ <u>27</u> requires that the auditor comply with relevant ethical requirements, including those pertaining to independence, relating to financial statement audit engagements, <u>including those requirements pertaining to independence</u>. Relevant ethical requirements may vary depending on the nature and circumstances of the engagement. For example, certain requirements related to independence may be applicable only when performing audits of listed entities. ISA <u>depository institutions or employee benefit plans. AU-C section 600</u> includes additional requirements and guidance to those in this ISA <u>SAS</u> regarding communications about relevant ethical requirements with component auditors.</p>	<p>To clarify; no change in application intended</p> <p>Specific to AS jurisdiction</p>
<p>A39. Based on the nature and circumstances of the audit engagement, certain law, regulation, or aspects of relevant ethical requirements, such as those pertaining to non-compliance with laws or regulations, may be relevant to the engagement, (for example, laws or regulations dealing with money laundering, corruption, or bribery).</p>	
<p>A40. The firm's information system and the resources provided by the firm may assist the engagement team in understanding and fulfilling relevant ethical requirements applicable to the nature and circumstances of the audit engagement. For example, the firm may <u>do the following</u>:</p>	
<ul style="list-style-type: none"> • Communicate the independence requirements to engagement teams. 	
<ul style="list-style-type: none"> • Provide training for engagement teams on relevant ethical requirements. 	
<ul style="list-style-type: none"> • Establish manuals and guides (i.e. that is, <u>intellectual resources</u>) containing the provisions of the relevant ethical requirements and guidance on how they are applied in the nature and circumstances of the firm and its engagements. 	

²⁸ ~~ISA 200, paragraphs 14 and A16–A19~~

²⁷ Paragraphs .16 and .A15–.A21 of AU-C section 200.

<ul style="list-style-type: none"> • Assign personnel to manage and monitor compliance with relevant ethical requirements (e.g., ISQM for example, SQMS No. 1 requires that the firm obtains, at least annually, a documented confirmation of compliance with the independence requirements from all personnel required by relevant ethical requirements to be independent) or provide consultation on matters related to relevant ethical requirements. 	
<ul style="list-style-type: none"> • Establish policies or procedures for engagement team members to communicate relevant and reliable information to appropriate parties within the firm or to the engagement partner, such as policies or procedures for engagement teams to: 	
<ul style="list-style-type: none"> <ul style="list-style-type: none"> ○ communicate information about client engagements and the scope of services, including non-assurance services, to enable the firm to identify threats to independence during the period of the engagement and during the period covered by the subject matter. 	
<ul style="list-style-type: none"> <ul style="list-style-type: none"> ○ communicate circumstances and relationships that may create a threat to independence, so that the firm can evaluate whether such a threat is at an acceptable level and, if it is not, address the threat by eliminating it or reducing it to an acceptable level. 	
<ul style="list-style-type: none"> <ul style="list-style-type: none"> ○ promptly communicate any breaches of the relevant ethical requirements, including those related to independence. 	
<p>A41. The engagement partner may take into account the information, communication, and resources described in paragraph A4039 when determining whether the engagement partner may depend on the firm’s policies or procedures in complying with relevant ethical requirements.</p>	
<p>A42. Open and robust communication between the members of the engagement team about relevant ethical requirements may also assist in:</p>	
<ul style="list-style-type: none"> • drawing the attention of engagement team members to relevant ethical requirements that may be of particular significance to the audit engagement; and 	
<ul style="list-style-type: none"> • keeping the engagement partner informed about matters relevant to the engagement team’s understanding and fulfillment of relevant ethical requirements and the firm’s related policies or procedures. 	
<p>Identifying and Evaluating Threats to Compliance With Relevant Ethical Requirements (Ref: par. 17–18)</p>	
<p>A43. In accordance with ISQM/SQMS No. 1, the firm’s responses to address the quality risks in relation to relevant ethical requirements, including those related to independence for engagement team members, include policies or</p>	

<p>procedures for identifying, evaluating, and addressing threats to compliance with the relevant ethical requirements.</p>	
<p>A44. Relevant ethical requirements may contain provisions regarding the identification and evaluation of threats and how they are to be dealt with. For example, the IESBA Code explains that a self-interest threat to compliance with the fundamental principle of professional competence and due care may arise if the fee quoted for an audit engagement is so low that it might be difficult to perform the engagement in accordance with professional standards“General Requirements for Performing Nonattest Services” interpretation (ET sec. 1.295.040) of the “Independence Rule” in the AICPA code provides guidance regarding safeguards for reducing threats to independence to an acceptable level when performing nonattest services for an attest client.”²⁹</p>	<p>Specific to ASB jurisdiction</p>
<p><i>Breaches of Relevant Ethical Requirements (Ref: par. 19)</i></p>	
<p>A45. In accordance with ISQMSSQMS No. 1, the firm is required to establish policies or procedures for identifying, communicating, evaluating, and reporting of any breaches of relevant ethical requirements and appropriately responding to the causes and consequences of the breaches in a timely manner.</p>	
<p><i>Taking Appropriate Action (Ref: par. 20)</i></p>	
<p>A46. Examples of appropriate actions may include, for example the following:</p>	
<ul style="list-style-type: none"> • Following the firm’s policies or procedures regarding breaches of relevant ethical requirements, including communicating to or consulting with the appropriate individuals so that appropriate action can be taken, including as applicable, disciplinary action(s). 	
<ul style="list-style-type: none"> • Communicating with those charged with governance. 	
<ul style="list-style-type: none"> • Communicating with regulatory authorities or professional bodies. In some circumstances, communication with regulatory authorities may be required by law or regulation. 	
<ul style="list-style-type: none"> • Seeking legal advice. 	
<ul style="list-style-type: none"> • Withdrawing from the audit engagement; when withdrawal is possible under applicable law or regulation. 	

²⁹ ~~IESBA Code, paragraph 330.3 A2~~

<p>Prior to Dating the Auditor’s Report (Ref: par. 21)</p>	
<p>A47. ISA AU-C section 700 (Revised), Forming an Opinion and Reporting on Financial Statements, requires that the auditor’s report include a statement that the auditor is independent of the entity in accordance with the relevant ethical requirements relating to the audit, and that the auditor has fulfilled the auditor’s other ethical responsibilities in accordance with these requirements.^{30 28} Performing the procedures required by paragraphs 16–21 of this ISA <u>SAS</u> provides the basis for these statements in the auditor’s report.</p>	
<p>Considerations Specific to Public Sector Entities <u>Governmental Audit Organizations</u></p>	
<p>A48. Statutory measures Law or regulation may provide safeguards for the independence of public sector <u>governmental audit organizations and the auditors they employ.</u> However, public sector auditors or audit firms carrying out public sector audits on behalf of <u>in the absence of law or regulation, governmental audit organizations may establish supplemental safeguards to assist</u> the statutory auditor may, depending on the terms of the mandate in a particular jurisdiction, need to adapt their approach to promote compliance with paragraph 16. This may include, where the public sector auditor’s mandate or audit organization in maintaining independence. Additionally, when law or regulation does not permit withdrawal from the <u>audit engagement,</u> disclosure through a public <u>the auditor may disclose in the auditor’s report of</u> the circumstances that have arisen that would, if they were in the private sector, lead affecting the auditor to withdraw’s independence.</p>	<p>Specific to ASB jurisdiction</p>
<p>Acceptance and Continuance of Client Relationships and Audit Engagements (Ref: par. 22–24)</p>	
<p>A49. ISQM <u>SQMS No. 1</u> requires the firm to establish quality objectives that address the acceptance and continuance of client relationships and specific engagements.</p>	
<p>A50. Information such as the following may assist the engagement partner in determining whether the conclusions reached regarding the acceptance and continuance of client relationships and audit engagements are appropriate:</p>	
<ul style="list-style-type: none"> • The integrity and ethical values of the principal owners, key management, and those charged with governance of the entity; 	
<ul style="list-style-type: none"> • Whether sufficient and appropriate resources are available to perform the engagement; 	
<ul style="list-style-type: none"> • Whether management and those charged with governance have acknowledged their responsibilities in relation to the engagement; 	
<ul style="list-style-type: none"> • Whether the engagement team has the competence and capabilities, including sufficient time, to perform the engagement; <p>and</p>	

³⁰ ~~ISA 700 (Revised),~~ ²⁸ Paragraph 28 ~~(c of AU-C)~~ section 700.

<ul style="list-style-type: none"> • Whether significant matters that have arisen during the current or previous engagement have implications for continuing the engagement. 	
<p>A51. Under ISQM<u>SQMS No.</u> 1, for acceptance and continuance decisions, the firm is required to make judgments about the firm's ability to perform the engagement in accordance with professional standards and applicable legal and regulatory requirements. The engagement partner may use the information considered by the firm in this regard in determining whether the conclusions reached regarding the acceptance and continuance of client relationships and audit engagements are appropriate. If the engagement partner has concerns regarding the appropriateness of the conclusions reached, the engagement partner may discuss the basis for those conclusions with those involved in the acceptance and continuance process.</p>	
<p>A52. If the engagement partner is directly involved throughout the firm's acceptance and continuance process, the engagement partner will be aware of the information obtained or used by the firm in reaching the related conclusions. Such direct involvement may also provide a basis for the engagement partner's determination that the firm's policies or procedures have been followed and that the conclusions reached are appropriate.</p>	
<p>A53. Information obtained during the acceptance and continuance process may assist the engagement partner in complying with the requirements of this ISASAS and making informed decisions about appropriate courses of action. Such information may include <u>the following</u>:</p>	
<ul style="list-style-type: none"> • Information about the size, complexity, and nature of the entity, including whether it is a group audit, the industry in which it operates, and the applicable financial reporting framework; 	
<ul style="list-style-type: none"> • The entity's timetable for reporting, such as at interim and final stages; 	
<ul style="list-style-type: none"> • In relation to group audits, the nature of the control relationships between the parent and its components; and 	
<ul style="list-style-type: none"> • Whether there have been changes in the entity or in the industry in which the entity operates since the previous audit engagement that may affect the nature of resources required, as well as the manner in which the work of the engagement team will be directed, supervised, and reviewed. 	
<p>A54. Information obtained during acceptance and continuance may also be relevant in complying with the requirements of other ISAs<u>AU-C sections</u>, as well as this ISASAS, for example, with respect to <u>the following</u>:</p>	

<ul style="list-style-type: none"> Establishing an understanding of the terms of the audit engagement, as required by ISAAU-C section 210;³⁴ Terms of Engagement²⁹ 	
<ul style="list-style-type: none"> Identifying and assessing risks of material misstatement, whether due to error or fraud, in accordance with ISAAU-C section 315 (Revised 2019) and ISAAU-C section 240;³² Consideration of Fraud in a Financial Statement Audit 	
<ul style="list-style-type: none"> Understanding the group, its components, and their environments, in the case of an audit of group financial statements in accordance with ISAAU-C section 600, and directing, supervising, and reviewing the work of component auditors; 	
<ul style="list-style-type: none"> Determining whether, and how, to involve an auditor's expertspecialist in accordance with ISAAU-C section 620; and 	
<ul style="list-style-type: none"> The entity's governance structure in accordance with ISAAU-C section 260 (Revised)³³, The Auditor's Communication With Those Charged With Governance, and ISAAU-C section 265.³⁴ Communicating Internal Control Related Matters Identified in an Audit 	
<p>A55. Law, regulation, or relevant ethical requirements may require the successor auditor to request, prior to accepting the audit engagement, the predecessor auditor to provide known information regarding any facts or circumstances that, in the predecessor auditor's judgment, the successor auditor needs to be aware of before deciding whether to accept the engagement. In some circumstances, the predecessor auditor may be required, on request by the proposed successor auditor, to provide information regarding identified or suspected non-compliance with laws and regulations to the proposed successor auditor. For example, if the predecessor auditor has withdrawn from the engagement as a result of identified or suspected non-compliance with laws and regulations, the IESBA Code requires that the predecessor auditor, on request by a proposed successor auditor, provide all relevant facts and other information concerning such non-compliance that, in the predecessor auditor's opinion, the proposed successor auditor needs to be aware of before deciding whether to accept the audit appointment.</p>	<p>Specific to ASB jurisdiction</p>
<p>A56. In circumstances whenin which the firm is obligated by law or regulation to accept or continue an audit engagement, the engagement partner may take</p>	

³⁴ ISA 210, *Agreeing the Terms of Audit Engagements*, paragraph 9

²⁹ Paragraph .09 of AU-C section 210, *Terms of Engagement*.

³² ISA 240, *The Auditor's Responsibilities Relating to Fraud in an Audit of Financial Statements*

³³ ISA 260 (Revised), *Communication with Those Charged with Governance*

³⁴ ISA 265, *Communicating Deficiencies in Internal Control to Those Charged with Governance and Management*

<p>into account information obtained by the firm about the nature and circumstances of the engagement.</p>	
<p>A57. In deciding on the necessary action, the engagement partner and the firm may conclude that it is appropriate to continue with the audit engagement and, if so, determine what additional steps are necessary at the engagement level (e.g. for example, the assignment of more staff or staff with specific expertise). If the engagement partner has further concerns or is not satisfied that the matter has been appropriately dealt with resolved, the firm’s policies or procedures for resolving differences of opinion may be applicable.</p>	
<p>Considerations Specific to Public Sector Entities Governmental Audit Organizations (Ref: par. 22–24)</p>	
<p>A58. In When the public sector, auditors auditor is a government audit organization, the auditor may be appointed in accordance with statutory procedures law or regulation, and the public sector auditor may not need to establish all policies or procedures regarding the acceptance and continuance of audit engagements. Nevertheless, the requirements and considerations for the acceptance and continuance of client relationships and engagements as set out in paragraphs 22–24 and A4948–A5756 may be valuable to public sector such auditors in performing risk assessments and in carrying out reporting responsibilities.</p>	<p>Specific to ASB jurisdiction</p>
<p>Engagement Resources (Ref: par. 25–28)</p>	
<p>A59. Under ISQMS SQMS No. 1, the resources assigned or made available by the firm to support the performance of audit engagements include:</p>	
<ul style="list-style-type: none"> • human resources; 	
<ul style="list-style-type: none"> • technological resources; and 	
<ul style="list-style-type: none"> • intellectual resources. 	
<p>A60. Resources for an audit engagement are primarily assigned or made available by the firm, although there may be circumstances when in which the engagement team directly obtains resources for the audit engagement. For example, this may be the case when a component auditor is required by statute, regulation, or for another reason to express an audit opinion on the financial statements of a component, and the component auditor is also appointed by component management to perform audit procedures on behalf of the group engagement team. ³⁵ 30 In such circumstances, the firm’s policies or procedures may require the engagement partner to take different actions, such as requesting information from the component auditor, to determine whether sufficient and appropriate resources are assigned or made available.</p>	
<p>A61. A relevant consideration for the engagement partner, in complying with the requirements in paragraphs 25 and 26, may be whether the resources assigned or made available to the engagement team enable fulfillment of</p>	

³⁵ ~~ISA 600, paragraph 3~~

³⁰ See paragraph .03 of AU-C section 600, *Special Considerations — Audits of Group Financial Statements (Including the Work of Component Auditors)*.

<p>relevant ethical requirements, including ethical principles such as professional competence and due care.</p>	
<p>Human Resources</p>	
<p>A62. Human resources include members of the engagement team (see also paragraphs A5, <u>and</u> A15–A21) and, <u>where</u><u>when</u> applicable, an auditor’s external expert<u>specialist</u> and individuals from within the entity’s internal audit function who provide direct assistance on the audit.</p>	
<p>Technological Resources</p>	
<p>A63. The use of technological resources on the audit engagement may assist the auditor in obtaining sufficient appropriate audit evidence. Technological <u>resources may include</u> tools may<u>that</u> allow the auditor to more effectively and efficiently manage the audit. Technological tools may also allow the auditor to evaluate large amounts of data more easily to, for example, provide deeper insights, identify unusual trends, or more effectively challenge management’s assertions, which enhances the ability of the auditor to exercise professional skepticism. Technological tools may also be used to conduct meetings and provide communication tools to the engagement team. Inappropriate use of such technological resources may, however, increase the risk of overreliance on the information produced for decision <u>-</u>making purposes, or may create threats to complying with relevant ethical requirements, for example, requirements related to confidentiality.</p>	<p>To clarify; no change in application intended</p>
<p>A64. The firm’s policies or procedures may include required considerations or responsibilities for the engagement team when using firm <u>-</u>approved technological tools to perform audit procedures and may require, <u>depending on the tool used</u>, the involvement of individuals with specialized skills or expertise in evaluating or analyzing the output.</p>	<p>To clarify; no change in application intended</p>
<p>A65.When the engagement partner requires individuals from another firm to use specific automated tools and techniques when performing audit procedures, communications with those individuals may indicate that the use of such automated tools and techniques needs to comply with the engagement team’s instructions.</p>	
<p>A66. The firm’s policies or procedures may specifically prohibit the use of certain IT applications or features of IT applications (e-g-for example, software that has not yet been specifically approved for use by the firm). Alternatively, the firm’s policies or procedures may require the engagement team to take certain actions before using an IT application that is not firm- approved to determine it is appropriate for use, for example, <u>by requiring</u>:</p>	
<ul style="list-style-type: none"> • the engagement team to have appropriate competence and capabilities to use the IT application<u>technological resource</u>. 	
<ul style="list-style-type: none"> • testing <u>of</u> the operation and security of the IT application. 	
<ul style="list-style-type: none"> • specific documentation to be included in the audit file. 	
<p>A67. The engagement partner may exercise professional judgment in considering whether the use of an IT application on the audit engagement is</p>	

<p>appropriate in the context of the engagement, and if so, how the IT application is to be used. Factors that may be considered in determining whether a particular IT application that has not been specifically approved for use by the firm, is appropriate for use in the audit engagement include whether:</p>	
<ul style="list-style-type: none"> • use and security of the IT application complies<u>comply</u> with the firm's policies or procedures. 	
<ul style="list-style-type: none"> • the IT application operates as intended. 	
<ul style="list-style-type: none"> • personnel have the competence and capabilities required to use the IT application. 	
<p><i>Intellectual Resources</i></p>	
<p>A68. Intellectual resources include, for example, audit methodologies, implementation tools, auditing guides, model programs, templates, checklists, or forms.</p>	
<p>A69. The use of intellectual resources on the audit engagement may facilitate the consistent application and understanding of professional standards, law and regulation, and related firm policies or procedures. For this purpose, the engagement team may be required, in accordance with the firm's policies or procedures, to use the firm's audit methodology and specific tools and guidance. The engagement team may also consider whether the use of other intellectual resources is appropriate and relevant based on the nature and circumstances of the engagement, for example, an industry <u>s</u>pecific methodology or related guides and performance aids.</p>	
<p><i>Sufficient and Appropriate Resources to Perform the Engagement (Ref: par. 25)</i></p>	
<p>A70. In determining whether sufficient and appropriate resources to perform the engagement have been assigned or made available to the engagement team, ordinarily, the engagement partner may depend on the firm's related policies or procedures (including resources) as described in paragraph A6. For example, based on information communicated by the firm, the engagement partner may be able to depend on the firm's technological development, implementation, and maintenance programs when using firm-approved technology to perform audit procedures.</p>	
<p><u>A71. The engagement partner may find it necessary to seek input from others with responsibilities for direction, supervision, and review to make the determinations required by paragraphs 25–27 of this SAS.</u></p>	<p>To clarify; no change in application intended</p>
<p><i>Competence and Capabilities of the Engagement Team (Ref: par. 26)</i></p>	
<p>A7172. When determining that the engagement team has the appropriate competence and capabilities, the engagement partner may take into consideration such matters as the team's:</p>	

<ul style="list-style-type: none"> understanding of, and practical experience with, audit engagements of a similar nature and complexity through appropriate training and participation. 	
<ul style="list-style-type: none"> understanding of professional standards and applicable legal and regulatory requirements. 	
<ul style="list-style-type: none"> expertise in specialized areas of accounting or auditing. 	
<ul style="list-style-type: none"> expertise in IT used by the entity or automated tools or techniques that are to be used by the engagement team in planning and performing the audit engagement. 	
<ul style="list-style-type: none"> knowledge of relevant industries in which the entity being audited operates. 	
<ul style="list-style-type: none"> ability to exercise professional skepticism and professional judgment. 	
<ul style="list-style-type: none"> understanding of the firm’s policies or procedures. 	
<p>A7273. Internal auditors and an auditor’s external expertspecialist are not members of the engagement team. ISAAU-C section 610 (Revised 2013)³⁶³¹ and ISAAU-C section 620³⁷³² include requirements and guidance relating to the assessment of the competence and capabilities of internal auditors and an auditor’s external expertspecialist, respectively.</p>	ASB preferred wording
<p>Project Management</p>	
<p>A7374. In situations wherein which there are many engagement team members, for example, in an audit of a larger or more complex entity, the engagement partner may involve an individual who has specialized skills or knowledge in project management, supported by appropriate technological and intellectual resources of the firm. Conversely, in an audit of a less complex entity with few engagement team members, project management may be achieved by a member of the engagement team through less formal means.</p>	AICPA style
<p>A7475. Project management techniques and tools may support the engagement team in managing the quality of the audit engagement by, for example:</p>	
<ul style="list-style-type: none"> increasing the engagement team’s ability to exercise professional skepticism through alleviating budget or time constraints that may otherwise impede the exercise of professional skepticism; 	
<ul style="list-style-type: none"> facilitating timely performance of audit work to effectively manage time constraints at the end of the audit process when more difficult or contentious matters may arise; 	

³⁶ ISA 610 (Revised 2013), ³¹ Paragraph 45.13 of AU-C section 610.

³⁷ ISA 620, paragraph 9. ³⁸ See ISA 300, ³² Paragraph 9.09 of AU-C section 620.

<ul style="list-style-type: none"> • monitoring the progress of the audit against the audit plan,^{38 33} including the achievement of key milestones, which may assist the engagement team in being proactive in identifying the need for making timely adjustments to the audit plan and the assigned resources;or 	
<ul style="list-style-type: none"> • facilitating communication among members of the engagement team, for example, coordinating arrangements with component auditors and auditor's experts. 	
<p><i>Insufficient or Inappropriate Resources (Ref: par. 27)</i></p>	
<p>A7576.ISQM <u>SQMS No. 1</u> addresses the firm's commitment to quality through its culture that exists throughout the firm, which recognizes and reinforces the firm's role in serving the public interest by consistently performing quality engagements, and the importance of quality in the firm's strategic decisions and actions, including the firm's financial and operational priorities. ISQM<u>SQMS No. 1</u> also addresses the firm's responsibilities for planning for resource needs, and obtaining, allocating, or assigning resources in a manner that is consistent with the firm's commitment to quality. However, in certain circumstances, the firm's financial and operational priorities may place constraints on the resources assigned or made available to the engagement team. In such circumstances, these constraints do not override the engagement partner's responsibility for achieving quality at the engagement level, including for determining that the resources assigned or made available by the firm are sufficient and appropriate to perform the audit engagement.</p>	
<p>A7677. In an audit of group financial statements, when there are insufficient or inappropriate resources in relation to work being performed at a component by a component auditor, the engagement partner may discuss the matter with the component auditor, management, or the firm to make sufficient and appropriate resources available.</p>	
<p>A7778. The engagement partner's determination of whether additional engagement level resources are required is a matter of professional judgment and is influenced by the requirements of this ISAS<u>SAS</u> and the nature and circumstances of the audit engagement. As described in paragraph A11, in certain circumstances, the engagement partner may determine that the firm's responses to quality risks are ineffective in the context of the specific engagement, including that certain resources assigned or made available to the engagement team are insufficient. In those circumstances, the engagement partner is required to take appropriate action, including communicating such information to the appropriate individuals in accordance with paragraph 27 and paragraph 39(c). For example, if an audit software program provided by the firm has not incorporated new or revised audit procedures in respect of<u>regarding</u> recently issued industry regulation, timely communication of such information to the firm enables the firm to take steps to update and reissue the software promptly or to provide an alternative resource that enables the engagement team to comply with the new regulation in the performance of the audit engagement.</p>	

³³ See paragraph .09 of AU-C section 300.

<p>A7879. If the resources assigned or made available are insufficient or inappropriate in the circumstances of the engagement and additional or alternative resources have not been made available, appropriate actions may include <u>the following</u>:</p>	
<ul style="list-style-type: none"> • Changing the planned approach to the nature, timing, and extent of direction, supervision, and review (see also paragraph A94). 	
<ul style="list-style-type: none"> • Discussing an extension to reporting deadlines with management or those charged with governance, when an extension is possible under applicable law or regulation. 	
<ul style="list-style-type: none"> • Following the firm’s policies or procedures for resolving differences of opinion if the engagement partner does not obtain the necessary resources for the audit engagement. 	
<ul style="list-style-type: none"> • Following the firm’s policies or procedures for withdrawing from the audit engagement, when withdrawal is possible under applicable law or regulation. 	
<p>Considerations Specific to Public Sector <u>Audits of Governmental</u> Entities (Ref: par. 25–28)</p>	
<p>A7980. In the public sector, specialized <u>For audits of governmental entities, competence may include</u> skills may be that are necessary to discharge the terms of the audit mandate in a particular jurisdiction. Such skills may include <u>comply with applicable law or regulation, such as knowledge of <i>Government Auditing Standards</i> and</u> an understanding of the applicable reporting arrangements <u>requirements</u>, including reporting to the legislature or other governing body or reporting in the public interest. The wider scope of a public sector <u>governmental</u> audit may include, for example, some aspects of performance auditing <u>additional requirements with respect to detecting misstatements that result from violations of provisions of contracts or grant agreements that could have a direct and material effect on the determination of financial statement amounts or the need to examine and report on internal control over financial reporting or compliance.</u></p>	<p>Specific to ASB jurisdiction</p>
<p>Engagement Performance</p>	
<p>Scalability (Ref: par. 29)</p>	
<p>A8081. When an audit is not carried out entirely by the engagement partner, or in an audit of an entity whose nature and circumstances are more complex, it may be necessary for the engagement partner to assign direction, supervision, and review to other members of the engagement team. However, as part of the engagement partner’s overall responsibility for managing and achieving quality on the audit engagement and to be sufficiently and appropriately involved, the engagement partner is required to determine that the nature, timing, and extent of direction, supervision, and review is undertaken in accordance with paragraph 30. In such circumstances, personnel or members of the engagement team, including component auditors, may provide information to the engagement partner to enable the engagement partner to make the determination required by paragraph 30.</p>	

<i>Direction, Supervision, and Review (Ref: par. 30)</i>	
<p>A8182. Under ISQMS<u>SQMS</u> No. 1, the firm is required to establish a quality objective that addresses the nature, timing, and extent of the direction and supervision of engagement teams and review of their work. ISQMS<u>SQMS</u> No. 1 also requires that such direction, supervision, and review is<u>be</u> planned and performed on the basis that the work performed by less experienced members of the engagement team is<u>be</u> directed, supervised, and reviewed by more experienced engagement team members.</p>	
<p>A8283. Direction and supervision of the engagement team and the review of the work of the engagement team are firm-level responses that are implemented at the engagement level, of which the nature, timing, and extent may be further tailored by the engagement partner in managing the quality of the audit engagement. Accordingly, the approach to direction, supervision, and review will vary from one engagement to the next, taking into account the nature and circumstances of the engagement. The approach will generally include a combination of addressing the firm's policies or procedures and engagement-specific responses.</p>	
<p>A8384. The approach to the direction and supervision of the members of the engagement team and the review of their work provides support for the engagement partner in fulfilling the requirements of this ISA,<u>SAS</u> and in concluding that the engagement partner has been sufficiently and appropriately involved throughout the audit engagement in accordance with paragraph 40.</p>	
<p>A8485. Ongoing discussion and communication among members of the engagement team allows less experienced engagement team members to raise questions with more experienced engagement team members (including the engagement partner) in a timely manner and enables effective direction, supervision, and review in accordance with paragraph 30.</p>	
<p><i>Direction</i></p>	
<p>A8586. Direction of the engagement team may involve informing the members of the engagement team of their responsibilities, such as <u>the following</u>:</p>	
<ul style="list-style-type: none"> • Contributing to the management and achievement of quality at the engagement level through their personal conduct, communication, and actions- 	
<ul style="list-style-type: none"> • Maintaining a questioning mind and being aware of unconscious or conscious auditor biases in exercising<u>maintaining</u> professional skepticism when gathering and evaluating audit evidence (see paragraph A35)- 	<p>ASB preferred word</p>
<ul style="list-style-type: none"> • Fulfilling relevant ethical requirements- 	
<ul style="list-style-type: none"> • The responsibilities of respective partners when more than one partner is involved in the conduct of an audit engagement- 	
<ul style="list-style-type: none"> • The responsibilities of respective engagement team members to perform audit procedures and of more experienced engagement 	

team members to direct, supervise, and review the work of less experienced engagement team members.	
<ul style="list-style-type: none"> Understanding the objectives of the work to be performed and the detailed instructions regarding the nature, timing, and extent of planned audit procedures as set forth in the overall audit strategy and audit plan. 	
<ul style="list-style-type: none"> Addressing threats to the achievement of quality, and the engagement team's expected response, for example, <u>the threat that</u> budget constraints or resource constraints should not result in the engagement team members <u>inappropriately</u> modifying planned audit procedures or failing to perform planned audit procedures. 	To clarify; no change in application intended
<i>Supervision</i>	
A8687. Supervision may include matters such as <u>the following</u> :	
<ul style="list-style-type: none"> Tracking the progress of the audit engagement, which includes monitoring: <ul style="list-style-type: none"> the progress against the audit plan; whether the objective of work performed has been achieved; and the ongoing adequacy of assigned resources. 	
<ul style="list-style-type: none"> Taking appropriate action to address issues arising during the engagement, including, for example, reassigning planned audit procedures to more experienced engagement team members when issues are more complex than initially anticipated. 	
<ul style="list-style-type: none"> Identifying matters for consultation or consideration by more experienced engagement team members during the audit engagement. 	
<ul style="list-style-type: none"> Providing coaching and on-the-job training to help engagement team members develop skills or competencies. 	
<ul style="list-style-type: none"> Creating an environment where engagement team members raise concerns without fear of reprisals. 	
<i>Review</i>	
A87. Review of the engagement team's work provides support for the conclusion that the requirements of this ISAS <u>SAS</u> have been addressed.	
A8889. Review of the engagement team's work consists of consideration of whether, for example:	

<ul style="list-style-type: none"> the work has been performed in accordance with the firm's policies or procedures, professional standards, and applicable legal and regulatory requirements; 	
<ul style="list-style-type: none"> significant matters have been raised for further consideration; 	
<ul style="list-style-type: none"> appropriate consultations have taken place, and the resulting conclusions have been documented and implemented; 	
<ul style="list-style-type: none"> there is a need to revise the nature, timing, and extent of work performed; 	
<ul style="list-style-type: none"> the work performed supports the conclusions reached and is appropriately documented;➤ 	
<ul style="list-style-type: none"> the evidence obtained is sufficient and appropriate to provide a basis for the auditor's opinion; and 	
<ul style="list-style-type: none"> the objectives of the audit procedures have been achieved. 	
<p>A8990. The firm's policies or procedures may contain specific requirements regarding:</p>	
<ul style="list-style-type: none"> the nature, timing, and extent of review of audit documentation; 	
<ul style="list-style-type: none"> different types of review that may be appropriate in different situations (e.g. for example, review of each individual working paper or selected working papers); and 	
<ul style="list-style-type: none"> which members of the engagement team are required to perform the different types of review. 	
<p><i>The Engagement Partner's Review (Ref: par. 30–34)</i></p>	
<p>A9091. <u>As required by AU-C section 300, the engagement partner reviews the overall audit strategy and audit plan.</u>³⁴ As required by ISA<u>AU-C section</u> 230, the engagement partner documents the date and extent of the review.^{38 35}</p>	<p>To clarify; no change in application intended</p>
<p>A9192. Timely review of documentation by the engagement partner at appropriate stages throughout the audit engagement enables significant matters to be resolved to the engagement partner's satisfaction on or before the date of the auditor's report. The engagement partner need not review all audit documentation.</p>	
<p>A92<u>The engagement partner exercises professional judgment in determining the extent of documentation to be reviewed, for example, when determining the</u></p>	<p>To clarify; no change in application intended</p>

³⁴ Paragraph .11 of AU-C section 300, as amended by this SAS.

³⁸ ~~ISA-230, paragraph 9(c)~~

³⁵ Paragraph .09c of AU-C section 230.

<p><u>nature and extent of the review of component auditor documentation in a group audit.</u></p>	
<p>A93. The engagement partner exercises professional judgment in identifying the areas of significant judgment made by the engagement team. The firm’s policies or procedures may specify certain matters that are commonly expected to be significant judgments. Significant judgments in relation to the audit engagement may include matters related to the overall audit strategy and audit plan for undertaking the engagement, the execution of the engagement, and the overall conclusions reached by the engagement team, for example. <u>Examples follow:</u></p>	
<ul style="list-style-type: none"> • Matters related to planning the engagement, such as matters related to determining materiality; 	
<ul style="list-style-type: none"> <ul style="list-style-type: none"> ○ The composition of the engagement team, including; 	
<ul style="list-style-type: none"> <ul style="list-style-type: none"> <ul style="list-style-type: none"> - personnel using expertise in a specialized area of accounting or auditing; 	
<ul style="list-style-type: none"> <ul style="list-style-type: none"> <ul style="list-style-type: none"> - the use of personnel from service delivery centers; 	
<ul style="list-style-type: none"> <ul style="list-style-type: none"> ○ The decision to involve an auditor’s expert<u>specialist</u>, including the decision to involve an external expert.<u>specialist</u> 	
<ul style="list-style-type: none"> • The engagement team's consideration of information obtained in the acceptance and continuance process and proposed responses to that information; 	
<ul style="list-style-type: none"> • The engagement team's risk assessment process, including situations wherein which consideration of inherent risk factors and the assessment of inherent risk requires significant judgment by the engagement team; 	
<ul style="list-style-type: none"> • The engagement team's consideration of related party relationships and transactions and disclosures; 	
<ul style="list-style-type: none"> • Results of the procedures performed by the engagement team on significant areas of the engagement, for example, conclusions in respect of<u>concerning</u> certain accounting estimates, accounting policies, or going concern considerations; 	
<ul style="list-style-type: none"> • The engagement team's evaluation of the work performed by experts<u>specialists</u> and conclusions drawn therefrom; 	
<ul style="list-style-type: none"> • In group audit situations; 	
<ul style="list-style-type: none"> <ul style="list-style-type: none"> ○ the proposed overall group audit strategy and group audit plan; 	
<ul style="list-style-type: none"> <ul style="list-style-type: none"> ○ decisions about the involvement of component auditors, including how to direct and supervise them and review their 	

work, including, for example, when there are areas of higher assessed risk of material misstatement of the financial information of a component; and	
<ul style="list-style-type: none"> ○ the evaluation of work performed by component auditors and the conclusions drawn therefrom; 	
<ul style="list-style-type: none"> • How matters affecting the overall audit strategy and audit plan have been addressed; 	
<ul style="list-style-type: none"> • The significance and disposition of corrected and uncorrected misstatements identified during the engagement; 	
<ul style="list-style-type: none"> • The proposed audit opinion and matters to be communicated in the auditor’s report, for example, key audit matters, or a “Material Uncertainty Related to Going Concern” paragraph; 	
A9394. The engagement partner exercises professional judgment in determining other matters to review, for example, based on:	
<ul style="list-style-type: none"> • the nature and circumstances of the audit engagement. 	
<ul style="list-style-type: none"> • which engagement team member performed the work. 	
<ul style="list-style-type: none"> • matters relating to recent inspection findings. 	
<ul style="list-style-type: none"> • the requirements of the firm’s policies or procedures. 	
<i>Nature, Timing, and Extent</i>	
A9495. The nature, timing, and extent of the direction, supervision, and review are required to be planned and performed in accordance with the firm’s policies or procedures, as well as professional standards and applicable legal and regulatory requirements. For example, the firm’s policies or procedures may include that the following:	
<ul style="list-style-type: none"> • Work planned to be performed at an interim date is to be directed, supervised, and reviewed at the same time as the performance of the procedures, rather than at the end of the period, so that any necessary corrective action can be taken in a timely manner. 	
<ul style="list-style-type: none"> • Certain matters are to be reviewed by the engagement partner, and the firm may specify the circumstances or engagements in which such matters are expected to be reviewed. 	

<p><i>Scalability</i></p>	
<p>A9596. The <u>following are examples of factors that may influence the firm's</u> approach to direction, supervision, and review may be tailored depending on, for example:</p>	<p>AICPA style</p>
<ul style="list-style-type: none"> • The engagement team member's previous experience with the entity and the area to be audited. For example, if the work related to the entity's information system is being performed by the same engagement team member who performed the work in the prior period and there are no significant changes to the information system, the extent and frequency of the direction and supervision of the engagement team member may be less, and the review of the related working papers may be less detailed. 	
<ul style="list-style-type: none"> • The complexity of the audit engagement. For example, if significant events have occurred that make the audit engagement more complex, the extent and frequency of the direction and supervision of the engagement team member may be greater, and the review of the related working papers may be more detailed. 	
<ul style="list-style-type: none"> • The assessed risks of material misstatement. For example, a higher assessed risk of material misstatement may require a corresponding increase in the extent and frequency of the direction and supervision of engagement team members and a more detailed review of their work. 	
<ul style="list-style-type: none"> • The competence and capabilities of the individual engagement team members performing the audit work. For example, less experienced engagement team members may require more detailed instructions and more frequent, or in-person, interactions as the work is performed. 	
<ul style="list-style-type: none"> • The manner in which the reviews of the work performed are expected to take place. For example, in some circumstances, remote reviews may not be effective in providing the necessary direction and may need to be supplemented by in-person interactions. 	
<ul style="list-style-type: none"> • The structure of the engagement team and the location of engagement team members. For example, direction and supervision of individuals located at service delivery centers and the review of their work may: 	
<ul style="list-style-type: none"> <ul style="list-style-type: none"> ○ be more formalized and structured than when members of the engagement team are all situated in the same location; or ○ 	

<ul style="list-style-type: none"> ○ use IT to facilitate the communication between the members of the engagement team. 	
<p>A9697. Identification of changes in the engagement circumstances may warrant reevaluation of the planned approach to the nature, timing, or extent of direction, supervision, or review. For example, if the assessed risk of material misstatement at the financial statement level increases because of a complex transaction, the engagement partner may need to change the planned level of review of the work related to the transaction.</p>	
<p>A9798. In accordance with paragraph 30(b), the engagement partner is required to determine that the approach to direction, supervision, and review is responsive to the nature and circumstances of the audit engagement. For example, if a more experienced engagement team member becomes unavailable to participate in the supervision and review of the engagement team, the engagement partner may need to increase the extent of supervision and review of the less experienced engagement team members.</p>	
<p>Review of Communications to Management, Those Charged With Governance, or Regulatory Authorities (Ref: par. 34)</p>	
<p>A9899. The engagement partner uses professional judgment in determining which written communications to review, taking into account the nature and circumstances of the audit engagement. For example, it may not be necessary for the engagement partner to review communications between the engagement team and management in the ordinary course of the audit.</p>	
<p>Consultation (Ref: par. 35)</p>	
<p>A99100. ISQM SQMS No. 1 requires the firm to establish a quality objective that addresses consultation on difficult or contentious matters and how the conclusions agreed are implemented. Consultation may be appropriate or required, for example, for:</p>	
<ul style="list-style-type: none"> • issues that are complex or unfamiliar (e.g. for example, issues related to an accounting estimate with a high degree of estimation uncertainty); 	
<ul style="list-style-type: none"> • significant risks; 	
<ul style="list-style-type: none"> • significant transactions that are outside the normal course of business for the entity; or that otherwise appear to be unusual; 	
<ul style="list-style-type: none"> • limitations imposed by management; and 	
<ul style="list-style-type: none"> • noncompliance with laws or regulations. 	
<p>A100101. Effective consultation on significant technical, ethical, and other matters within the firm or, where applicable, outside the firm, may be achieved when those consulted:</p>	
<ul style="list-style-type: none"> • are given all the relevant facts that will enable them to provide informed advice; and 	

<ul style="list-style-type: none"> • have appropriate knowledge, seniority, and experience. 	
<p>A104102. It may be appropriate for the engagement team, in the context of the firm’s policies or procedures, to consult outside the firm, for example, <u>in areas</u> where the firm lacks appropriate internal resources. The engagement team may take advantage of advisory services provided by firms, professional and regulatory bodies, or commercial organizations that provide relevant quality control services.</p>	<p>To clarify; no change in application intended</p>
<p>A102103. The need for consultation outside the engagement team on a difficult or contentious matter may be an indicator that the matter is a key audit matter.³⁹ <u>36</u></p>	
<p>Engagement Quality Review (Ref: par. 36)</p>	
<p>A103-ISQM104. <u>SQMS No. 1</u> contains requirements that the firm establish policies or procedures addressing engagement quality reviews in accordance with <u>ISQMSQMS No. 2</u>,⁴⁰ <u>Engagement Quality Reviews</u>³⁷ and requiring an engagement quality review for certain types of engagements.⁴⁴ <u>ISQM</u> ³⁸ <u>SQMS No. 2</u> deals with the appointment and eligibility of the engagement quality reviewer and the engagement quality reviewer’s responsibilities relating to performing and documenting an engagement quality review.</p>	
<p><i>Completion of the Engagement Quality Review Before Dating of the Auditor’s Report (Ref: par. 36(d))</i></p>	
<p>A104-105. <u>ISAAU-C section 700 (Revised)</u> requires the auditor’s report to be dated no earlier than the date on which the auditor has obtained sufficient appropriate audit evidence on which to base the auditor’s opinion on the financial statements.⁴²³⁹ If applicable to the audit engagement, <u>ISQMSQMS No. 2</u> and this <u>ISASAS</u> require that the engagement partner be precluded from <u>dating</u><u>releasing</u> the engagement report until notification has been received from the engagement quality reviewer that the engagement quality review is complete. For example, if the engagement quality reviewer has communicated to the engagement partner concerns about the significant judgments made by the engagement team or that the conclusions reached thereon were not appropriate, then the engagement quality review is not complete.⁴³⁴⁰</p>	<p>See paragraph 36d</p>
<p>A105106. An engagement quality review that is conducted in a timely manner at appropriate stages during the audit engagement may assist the</p>	

³⁹ ISA 701, paragraphs 9 and A14

³⁶ Paragraphs .09 and .A13b of AU-C section 701.

⁴⁰ ISQM³⁷ SQMS No. 2, Engagement Quality Reviews .

⁴⁴ ISQM 1, paragraph 34(f)

³⁸ Paragraph 35f of SQMS No. 1.

⁴² ISA 700 (Revised),³⁹ Paragraph 49.43 of AU-C section 700.

⁴³ ISQM 2,⁴⁰ Paragraph 2621b of SQMS No. 2.

<p>engagement team in promptly resolving matters raised to the engagement quality reviewer's satisfaction on or before the date of the auditor's report.</p>	
<p>A106107. Frequent communications between the engagement team and the engagement quality reviewer throughout the audit engagement may assist in facilitating an effective and timely engagement quality review. In addition to discussing significant matters with the engagement quality reviewer, the engagement partner may assign responsibility for coordinating requests from the engagement quality reviewer to another member of the engagement team.</p>	
<p><i>Differences of Opinion (Ref: par. 37–38)</i></p>	
<p>A107108. ISQMSQMS No. 1 requires the firm to establish a quality objective that addresses differences of opinion that arise within the engagement team, or between the engagement team and the engagement quality reviewer or individuals performing activities within the firm's system of quality management. ISQMSQMS No. 1 also requires that differences of opinion are<u>be</u> brought to the attention of the firm and resolved. <u>For example, a component auditor may be instructed to communicate differences of opinion to the group engagement team.</u></p>	<p>To clarify; no change in application intended</p>
<p>A109. A108In some circumstances, the engagement partner may not be satisfied with the resolution of the difference of opinion. In such circumstances, appropriate actions for the engagement partner may include, for example:-</p>	
<ul style="list-style-type: none"> • seeking legal advice; or 	
<ul style="list-style-type: none"> • withdrawing from the audit engagement, when withdrawal is possible under applicable law or regulation. 	
<p>Monitoring and Remediation (Ref: par. 39)</p>	
<p>A109. ISQM110. <u>SQMS No.</u> 1 sets out requirements for the firm's monitoring and remediation process. ISQM<u>SQMS No.</u> 1 requires the firm to communicate to engagement teams information about the firm's monitoring and remediation process to enable them to take prompt and appropriate action in accordance with their responsibilities.⁴⁴ Further, information provided by members of the engagement team may be used by the firm in the firm's monitoring and remediation process, and exercising professional judgment and <u>maintaining</u> professional skepticism while conducting the audit may assist the members of the engagement team in remaining alert for information that may be relevant to that process.</p>	
<p>A110111. Information provided by the firm may be relevant to the audit engagement when, for example, it relates to findings on another engagement performed by the engagement partner or other members of the engagement team, findings from the local firm office, or inspection results of previous audits of the entity.</p>	

⁴⁴ ISQM 1, paragraph 47

<p>A144112. In considering information communicated by the firm through its monitoring and remediation process and how it may affect the audit engagement, the engagement partner may consider the remedial actions designed and implemented by the firm to address identified deficiencies and, to the extent relevant to the nature and circumstances of the engagement, communicate accordingly to the engagement team. The engagement partner may also determine whether additional remedial actions are needed at the engagement level. For example, the engagement partner may determine that:</p>	<p>To clarify; no change in application intended</p>
<ul style="list-style-type: none"> • an auditor’s expert<u>specialist</u> is needed; or 	
<ul style="list-style-type: none"> • the nature, timing, and extent of direction, supervision, and review needs<u>need</u> to be enhanced in an area of the audit where deficiencies have been identified. 	<p>AICPA style</p>
<p>If an identified deficiency does not affect the quality of the audit (e.g. for example, if it relates to a technological resource that the engagement team did not use), then no further action may be needed.</p>	
<p>A112.113. <u>A</u> An identified deficiency in the firm’s system of quality management does not necessarily indicate that an audit engagement was not performed in accordance with professional standards and applicable legal and regulatory requirements, or that the auditor’s report was not appropriate in the circumstances.</p>	<p>To clarify; no change in application intended</p>
<p><i>Taking Overall Responsibility for Managing and Achieving Quality (Ref: par. 40)</i></p>	
<p>A113.ISQM114. <u>SQMS No. 1</u> requires the firm to establish a quality objective addressing the engagement team’s understanding and fulfillment of their responsibilities in connection with the engagement. ISQMS<u>SQMS No. 1</u> further requires that the quality objective include the overall responsibility of engagement partners for managing and achieving quality on the engagement and being sufficiently and appropriately involved throughout the engagement.</p>	
<p>A144115. Relevant considerations in addressing paragraph 40 include determining how the engagement partner has complied with the requirements of this ISAS<u>SAS</u>, given the nature and circumstances of the audit engagement and how the audit documentation evidences the engagement partner’s involvement throughout the audit engagement, as described in paragraph A118.</p>	
<p>A145116. Indicators that the engagement partner may not have been sufficiently and appropriately involved include, for example, <u>the following</u>:</p>	
<ul style="list-style-type: none"> • Lack of timely review by the engagement partner of the audit engagement planning, including reviewing the assessment of risks of material misstatement and the design of these responses to those risks. <u>toward the end of the audit</u> 	<p>To clarify; no change in application intended</p>

<ul style="list-style-type: none"> Evidence that those to whom tasks, actions or procedures have been assigned were not <u>assignees were not provided necessary instructions and relevant information, such as not being</u> adequately informed about the nature of their responsibilities and authority, the scope of the work being assigned, and the objectives thereof; and were not provided other necessary instructions and relevant information. 	<p>To clarify; no change in application intended</p>
<ul style="list-style-type: none"> A lack of evidence of the engagement partner's direction and supervision of the other members of the engagement team and the review of their work. 	
<p>A116117. If the engagement partner's involvement does not provide the basis for determining that the significant judgments made and the conclusions reached are appropriate, the engagement partner will not be able to reach the determination required by paragraph 40. In addition to taking <u>into</u> account of firm policies or procedures that may set forth the required actions to be taken in such circumstances, appropriate actions that the engagement partner may take, include, for example:</p>	
<ul style="list-style-type: none"> updating and changing the audit plan; 	
<ul style="list-style-type: none"> reevaluating the planned approach to the nature and extent of review and modifying the planned approach to increase the involvement of the engagement partner; or 	
<ul style="list-style-type: none"> consulting with personnel assigned operational responsibility for the relevant aspect of the firm's system of quality management. 	
<p>Documentation (Ref: par. 41)</p>	
<p>A117118. In accordance with <u>ISAAU-C section</u> 230,⁴⁵ <u>41</u> audit documentation provides evidence that the audit complies with the ISAs <u>GAAS</u>. However, it is neither necessary nor practicable for the auditor to document every matter considered, or professional judgment made, in an audit. Further, it is unnecessary for the auditor to document separately (<u>such</u> as in a checklist, for example) compliance with matters for which compliance is demonstrated by documents included within the audit file.</p>	
<p>A118119. Documentation of the performance of the requirements of this ISASAS, including evidencing the involvement of the engagement partner and the engagement partner's determination in accordance with paragraph 40, may be accomplished in different ways depending on the nature and circumstances of the audit engagement. For example <u>Examples follow:</u></p>	
<ul style="list-style-type: none"> Direction of the engagement team can be documented through sign-offs of the audit plan and project management activities; 	

⁴⁵ ~~ISA 230~~, ⁴¹ Paragraph 79 of AU-C section 230.

<ul style="list-style-type: none"> Minutes from formal meetings of the engagement team may provide evidence of the clarity, consistency, and effectiveness of the engagement partner’s communications and other actions in respect of regarding culture and expected behaviors that demonstrate the firm’s commitment to quality. 	
<ul style="list-style-type: none"> Agendas from discussions between the engagement partner and other members of the engagement team; and where, when applicable, the engagement quality reviewer, and related sign-offs and records of the time the engagement partner spent on the engagement, may provide evidence of the engagement partner’s involvement throughout the audit engagement and supervision of other members of the engagement team; of. 	
<ul style="list-style-type: none"> Sign-offs by the engagement partner and other members of the engagement team provide evidence that the working papers were reviewed. 	
<p>A119120. When dealing with circumstances that may pose risks to achieving quality on the audit engagement, the exercise of professional skepticism, and the documentation of the auditor’s consideration thereof, may be important. For example, if the engagement partner obtains information that may have caused the firm to decline the engagement (see paragraph 24), the documentation may include explanations of how the engagement team dealt with the circumstance.</p>	
<p>A120121. Documentation of consultations with other professionals that involve difficult or contentious matters that is sufficiently complete and detailed contributes to an understanding of:</p>	
<ul style="list-style-type: none"> the nature and scope of the issue on which consultation was sought; and 	
<ul style="list-style-type: none"> the results of the consultation, including any decisions taken, the basis for those decisions, and how they were implemented. 	

Document comparison by Workshare Compare on Tuesday, April 19, 2022
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Input:	
Document 1 ID	\\IAASB-International-Standard-Auditing-220-Revised.docx
Document 2 ID	2C QM SAS marked from January ASB meeting.docx
Rendering set	Standard

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Insertion	
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Total changes	2277

Quality Management Standards: What's Changing and What You Should Be Doing Now

What's changing?

In June 2022, the AICPA Auditing Standards Board (ASB) issued three interrelated standards on quality management (collectively, the QM standards). The new QM standards represent a significant change in how CPA firms will approach audit and assurance quality in the future, moving from a policies-based approach to a risk-based approach. Implementation of these new standards is required by the end of 2025.

The QM standards consist of the following:

- Statement on Quality Management (SQMS) No. 1, *A Firm's System of Quality Management*
 - SQMS No. 1 supersedes Statement on Quality Control Standards (SQCS) No. 8, *A Firm's System of Quality Control* (QC sec. 10) and requires the firm to design, implement and operate a system of quality management that is customized for the nature and circumstances of its accounting and auditing practice.
 - An engagement quality (EQ) review is a specified response the firm designs and implements to address quality risks, performed by an EQ reviewer at the engagement level on behalf of the firm. SQMS No. 1 requires that the firm determine when an EQ review is an appropriate response to quality risks.
- SQMS No. 2, *Engagement Quality Reviews*
 - SQMS No. 2 addresses the appointment and eligibility of the EQ reviewer; and performance of EQ reviews.
- Statement on Auditing Standards (SAS) No. 147, *Quality Management for An Engagement Conducted in Accordance With Generally Accepted Auditing Standards*
 - SAS No. 147 updates and supersedes AU-C section 220 and addresses quality management at the engagement level, focusing on the quality responsibilities of the engagement team and engagement partner.
- Statement on Standards for Accounting and Review Services (SSARS) No. 26, *Quality Management for an Engagement Conducted in Accordance With Statements on Standards for Accounting and Review Services*
 - SSARS No. 26 amends the SSARS to conform with SQMS Nos. 1 and 2.

Who's affected?

Every firm that performs engagements in accordance with the SASs, SSARSs, and SSAEs.

What are the key changes?

- New **risk-based approach**, incorporating a risk assessment process driving firms to focus on **quality management tailored** to their **circumstances**

Agenda Item 21 – QM Crosswalk

- **Revised components** of the system of quality management – two new components, including information and communication
- **More robust** leadership and governance requirements
- **Enhanced** monitoring and remediation process
- **New** requirements for networks and service providers

The Components of the System of Quality Management

The system of quality management comprises eight inter-related components as follows:

The firm's risk assessment process	A process established by the firm as part of the SQM	<ul style="list-style-type: none"> • The process the firm is required to follow in implementing the risk-based approach to quality management. • Consists of establishing quality objectives, identifying and assessing quality risks to the achievement of the quality objectives and designing and implementing responses to address the assessed quality risks.
Governance and leadership	Establishes the environment in which the SQM operates	<ul style="list-style-type: none"> • Deals with matters such as the firm's culture, leadership responsibility and accountability, the firm's organizational structure, assignment of roles and responsibilities and resource planning and allocation.
Relevant ethical requirements	Specific topic fundamental for engagement performance	<ul style="list-style-type: none"> • Deals with fulfilling relevant ethical requirements by the firm and its personnel. • Also deals with relevant ethical requirements to the extent that they apply to others external to the firm.
Acceptance and continuance of client relationships and specific engagements	Specific topic fundamental for engagement performance	<ul style="list-style-type: none"> • Deals with the firm's judgments about whether to accept or continue a client relationship or specific engagement.

Agenda Item 21 – QM Crosswalk

Engagement performance	Specific topic fundamental for engagement performance	<ul style="list-style-type: none"> Deals with the firm’s actions to promote and support the consistent performance of quality engagements, including through direction, supervision and review, consultation and communication and resolution of differences of opinion. Includes how the firm supports engagement teams in exercising professional judgment and, when applicable to the nature and circumstances of the engagement, exercising professional skepticism.
Resources	Enables operation of other components	<ul style="list-style-type: none"> Deals with obtaining, developing, using, maintaining, allocating and assigning resources in a timely manner to enable the design, implementation and operation of the SQM. Includes requirements related to technological, intellectual and human resources within the firm as well as those from service providers.
Information and communication	Enables operation of other components	<ul style="list-style-type: none"> Deals with obtaining, generating or using information regarding the SQM, and communicating information within the firm and to external parties on a timely basis to enable the design, implementation and operation of the SQM.
Monitoring and remediation process	A process established by the firm as part of the SQM	<ul style="list-style-type: none"> The process that: <ul style="list-style-type: none"> Provides the firm with relevant, reliable and timely information about the design, implementation and operation of the SQM; and Addresses taking appropriate actions to respond to deficiencies such that deficiencies are remediated on a timely basis.

Notable Differences and Enhancements:

Detailed Comparison of the Elements of Quality Control under QC 10 to the Components of Quality Management under SQMS No. 1

QC 10 - Elements of Quality Control	NEW SQMS No. 1 - Components of Quality Management	Notable Differences and Enhancements
No equivalent element in QC 10	The firm’s risk assessment process (<i>new!</i>)	<ul style="list-style-type: none"> New component requiring firms to establish a risk assessment process that supports the SQM

Agenda Item 21 – QM Crosswalk

QC 10 - Elements of Quality Control	NEW SQMS No. 1 - Components of Quality Management	Notable Differences and Enhancements
		<ul style="list-style-type: none"> • Firms should establish quality objectives, identify and assess quality risks, and design and implement responses to those risks • Firms should establish specified quality objectives for: <ul style="list-style-type: none"> ○ Governance and leadership ○ Relevant ethical requirements ○ Acceptance and continuance of client relationships and specific engagements ○ Engagement performance ○ Resources ○ Information and communication • Firms should establish policies or procedures to identify information that indicates additional quality objectives, additional or modified quality risks, or responses are needed due to the firm's circumstances
Leadership responsibilities for quality within the firm	Governance and leadership	<ul style="list-style-type: none"> • New focus on the role a firm's governance and leadership play in establishing an environment and culture that support the SQM • Firms should establish a culture that reinforces <ul style="list-style-type: none"> ○ serving the public interest, ○ the importance of professional ethics, values, and attitudes, ○ the responsibility of all personnel for quality, and ○ the importance of quality in strategic decisions and actions • New requirements that a firm's <ul style="list-style-type: none"> ○ leadership is not only responsible and accountable for quality, but also expected to demonstrate a commitment to quality through its actions and behaviors ○ organizational structure enables its SQM resources should be deployed in a manner that supports the firm's commitment to quality
Relevant ethical requirements	Relevant ethical requirements	<ul style="list-style-type: none"> • New emphasis on responsibilities for all relevant ethical requirements, including independence • New requirement that a firm ensures that others (e.g., network firms, individuals in the network, and service providers) who are involved in the firm's SQM or in performing engagements understand and fulfill relevant ethical requirements to which the firm and the firm's engagements are subject • Less prescription than in extant

Agenda Item 21 – QM Crosswalk

QC 10 - Elements of Quality Control	NEW SQMS No. 1 - Components of Quality Management	Notable Differences and Enhancements
Acceptance and continuance of client relationships and specific engagements	Acceptance and continuance of client relationships and specific engagements	<ul style="list-style-type: none"> • New requirement that emphasizes a firm's ability to perform an engagement in accordance with professional standards • Expanded emphasis on obtaining information about the nature and circumstances of an engagement along with the integrity and ethical values of the client • New requirement to ensure that financial and operational priorities do not inappropriately influence acceptance and continuance judgments
Engagement performance	Engagement performance	<ul style="list-style-type: none"> • New requirement that engagement teams understand and fulfill their professional responsibilities, including an engagement partner's overall responsibility for managing and achieving quality and being sufficiently and appropriately involved throughout an engagement • Revised requirement related to the direction and supervision of engagement teams and the review of work based on an engagement's nature and circumstances and the resources assigned or made available to the engagement team • New requirement related to the exercise of professional judgment and professional skepticism, when appropriate, by engagement teams • Various requirements related to engagement quality reviews (formerly engagement quality control reviews) have been relocated within SQMS No. 1 or moved to SQMS No. 2, <i>Engagement Quality Reviews</i>

Agenda Item 2I – QM Crosswalk

QC 10 - Elements of Quality Control	NEW SQMS No. 1 - Components of Quality Management	Notable Differences and Enhancements
Human resources	Resources	<ul style="list-style-type: none"> • New requirements related to technological and intellectual resources involved in a firm's SQM and the performance of engagements • New requirement that firms hire, develop, and retain personnel with the competence and capabilities to perform activities or carry out responsibilities within the SQM • New requirement that personnel demonstrate commitment to quality, be competent to perform their roles, and are held accountable through evaluations, compensation, promotion, and other incentives • New requirement that firms obtain individuals from external sources (e.g., a network firm, another network, or a service provider) when the firm does not have sufficient or appropriate personnel to operate the SQM or perform engagements
<i>No equivalent element in QC 10</i>	Information and communication (<i>New!</i>)	<ul style="list-style-type: none"> • New component requiring firms to establish information and communication processes that support the SQM • New requirement that the firm's information system incorporates reliable information from internal and external sources needed to support the SQM • New requirement that the firm's culture reinforce the responsibility for the sharing of information with one another and the firm • New requirement that information be exchanged throughout the firm so <ul style="list-style-type: none"> ○ personnel and engagement teams can understand and perform activities related to SQM and engagement ○ personnel and engagement teams communicate information to the firm related to the SQM • New requirement that information be communicated by the firm <ul style="list-style-type: none"> ○ to or within the firm's network or service providers to enable them to fulfill their responsibilities ○ to external parties as required by law, regulation, or professional standards for those parties to understand the SQM
Monitoring	The monitoring and remediation process	<ul style="list-style-type: none"> • Expanded and enhanced guidance throughout this component • New emphasis on the firm's remediation process

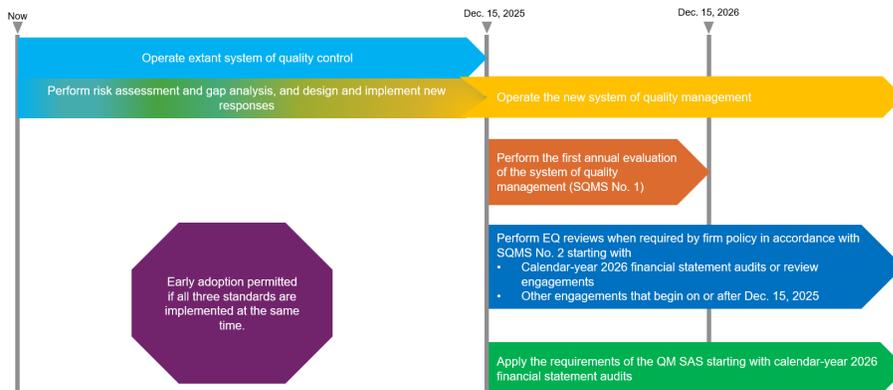
Agenda Item 2I – QM Crosswalk

		<ul style="list-style-type: none"> • New requirement that firms establish policies or procedures that address the objectivity of those performing monitoring activities • Introduction of the term “findings” in relation to information about the SQM that indicates a deficiency may exist • New requirements that the firm evaluate the severity and pervasiveness of identified deficiencies using a root cause analysis and design remedial actions that are responsive to the root cause analysis
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Effective date

Systems of quality management in compliance with SQMS No. 1 are required to be designed and implemented by Dec. 15, 2025. Evaluation of the system of quality management required by SQMS No. 1 is required to be performed within one year following Dec. 15, 2025.

Quality Management Standards Understanding Effective Dates



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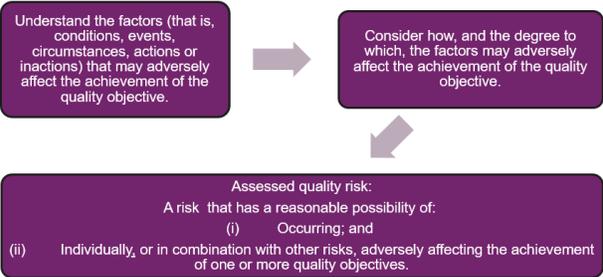
- December 2025 may seem really far off, but there's a reason the implementation period is so long: to allow you enough time to get the new system in place. It may be a big change, but done bit-by-bit over the next three years, it's manageable.
- The firm may start operation of all the new and revised policies or procedures at the effective date, or the firm may pilot test one or more components of the new SQM prior to the effective

Agenda Item 2I – QM Crosswalk

date. The pilot test may be conducted by the entire firm, or by a selection of engagements teams. The SQM would not be considered in operation until the firm has formally implemented and commenced operation of the new SQM in its entirety. This means that you can start to make changes—for example, implementing the new risk assessment process—and ask your peer reviewer to give you feedback on those changes. But you wouldn't get a matter for further consideration regarding those changes because your peer reviewer won't be measuring your system against the new standards until the firm formally implements them (which has to be no later than December 15, 2025).

What should I be doing now?

1. Understand the standards	<ul style="list-style-type: none">• Gain an overall understanding of the standards. The AICPA has developed the following resources to help you:<ul style="list-style-type: none">○ Executive Summaries of the standards○ Comparison of extant and new AICPA quality management standards○ AICPA webcasts○ AICPA Practice Aids○ CPE courses
2. Develop a plan for implementation	<ul style="list-style-type: none">• Determine who within the firm will take ownership and lead the implementation process<ul style="list-style-type: none">○ Note that SQMS No. 1 requires that the firm assign ultimate responsibility and authority for the SQM to the firm's managing partner, and assign operational responsibility for the SQM, and operational responsibility for specific aspects of the SQM to appropriate individuals within the firm• Determine the resources—human, intellectual and technical— needed for successful implementation.• Talk with your peer reviewer about your implementation plan. Note that your peer reviewer, to maintain independence, cannot be part of your system of quality management (just like you can't be part of your client's system of internal control over financial reporting) but may offer advice.• Determine how information will be documented• Develop a timeline.<ul style="list-style-type: none">○ Your firm may take a phased approach to implementation, building up to the effective date. For example, you may start by designing and implementing policies or procedures for one component at a time and begin operating those policies or procedures at various stages before the effective date.<ul style="list-style-type: none">▪ This phased approach may lessen the impact of many changes all at once.▪ Although your firm may implement policies or procedures before the effective date, the firm would not be considered as “early adopting” SQMS 1 because only a portion of the new SQM has been implemented.▪ The Appendix to this document includes an example timeline, indicating a phased approach performing the risk assessment, gap analysis, and designing/implementing responses for each component and then at the end re-evaluating the risk assessment, gap analysis, and the responses.

<p>3. Perform risk assessment</p>	<ul style="list-style-type: none"> Establish the quality objectives required by the standard. <ul style="list-style-type: none"> You may find it helpful to break the quality objectives into sub-objectives. The quality objectives are sufficiently comprehensive such that it is unlikely that you would find it necessary to establish additional quality objectives. Identify and assess quality risks. The following graphic explains how to identify quality risks. <p style="text-align: center;">Risk Assessment Process: Identify and Assess Quality Risks</p> <div style="text-align: center;">  <pre> graph TD A[Understand the factors (that is, conditions, events, circumstances, actions or inactions) that may adversely affect the achievement of the quality objective.] --> B[Consider how, and the degree to which, the factors may adversely affect the achievement of the quality objective.] B --> C[Assessed quality risk: A risk that has a reasonable possibility of: (i) Occurring; and (ii) Individually, or in combination with other risks, adversely affecting the achievement of one or more quality objectives.] </pre> </div> <ul style="list-style-type: none"> The assessment of identified quality risks does not require formal ratings or scores. Risk assessment is iterative, and as such, quality risks will be revisited throughout the process of implementation and maintenance of the SQM. The AICPA is exploring technology solutions to help you implement and manage your SQM, including tools to help identify and document quality risks and related responses. You may find it helpful to identify and assess quality risks one component at a time, and then revisit the components throughout the process. Consider any information the firm may have related to current quality risks (e.g., information provided to insurance carriers). Consider the inverse of the quality objectives as a quality risk (that is, the risk of not achieving the quality objective).
<p>4. Perform a gap analysis</p>	<ul style="list-style-type: none"> Based on the quality risks identified, map current controls—or, as SQMS No. 1 calls them, responses to quality risks. Identify quality risks without appropriate responses as well as any current responses that do not map to a quality risk. Take note of the specified responses within SQMS No. 1 that the firm is required to design and implement.
<p>5. Design and implement new responses for those risks that are not addressed</p>	<ul style="list-style-type: none"> Helpful resources for identifying potential responses to quality risks include AICPA Practice Aids, third-party providers of Quality Management Materials, and peer reviewers among others. You may decide that current responses that do not map to a risk are no longer necessary.

Agenda Item 2I – QM Crosswalk

<p>6. Prepare Documentation</p>	<ul style="list-style-type: none"> • The firm is not required to document the consideration of every condition, event, circumstance, action or inaction that may give rise to a quality risk. The documentation of the quality risks may include the reasons for the assessment given to the quality risks, that is, the considered occurrence and effect on the achievement of the quality objectives. • Documentation of the SQM will likely differ depending on the firm’s complexity. <ul style="list-style-type: none"> ○ A less complex firm may not need to have granular documentation, such as a matrix, that indicates the quality objective, the related quality risk(s), and the related responses to address those quality risks. This is because it may be obvious how the quality risks relate to the quality objectives, or how the responses address the quality risks. In these circumstances, the firm’s documentation may include lists of the quality objectives and quality risks, and a memorandum that explains the responses and how they address the quality risks. ○ As the complexity of the firm’s SQM increases, there may be a need to have more granular documentation that indicates the quality objective, the related quality risk(s), and the related responses to address those quality risks. This may become important when the volume of quality risks and related responses creates challenges in being able to identify which quality risks relate to which quality objectives, and which responses address which quality risks.
<p>7. Establish process for ongoing monitoring (adjusting for changes) and remediation</p>	<ul style="list-style-type: none"> • The monitoring and remediation process can be broken down into four aspects: <div style="text-align: center; margin: 10px 0;"> <pre> graph LR A[Design and Perform Monitoring Activities] --> B[Evaluate Findings and Identify Deficiencies, and Evaluate Identified Deficiencies] B --> C[Respond to Identified Deficiencies] C --> D[Communicate] </pre> </div> • Factors you are required to take into consideration when establishing monitoring activities are as follows: <ul style="list-style-type: none"> ○ The reasons for the assessments given to the quality risks ○ The design of the responses ○ The design of the firm’s risk assessment process and monitoring and remediation process ○ Changes in the SQM ○ Previous monitoring activity • The “information and communication” component plays an enabling role by providing ongoing information relevant to the SQM.
<p>8. Evaluate new system</p>	<p>Tips:</p> <ul style="list-style-type: none"> • A new requirement in SQMS No. 1 is for a firm leader to evaluate, at least annually, whether the SQM provides reasonable assurance that the objectives of the SQM are being met. The effective date for this evaluation is within one year of December 15, 2025. • Firm leadership is required to make this evaluation even in a peer review year. It is comparable to management’s assertion about its system of internal control over financial reporting (ICFR), which remains management’s responsibility regardless of whether an audit of an entity’s system of ICFR is performed.

RESOURCES

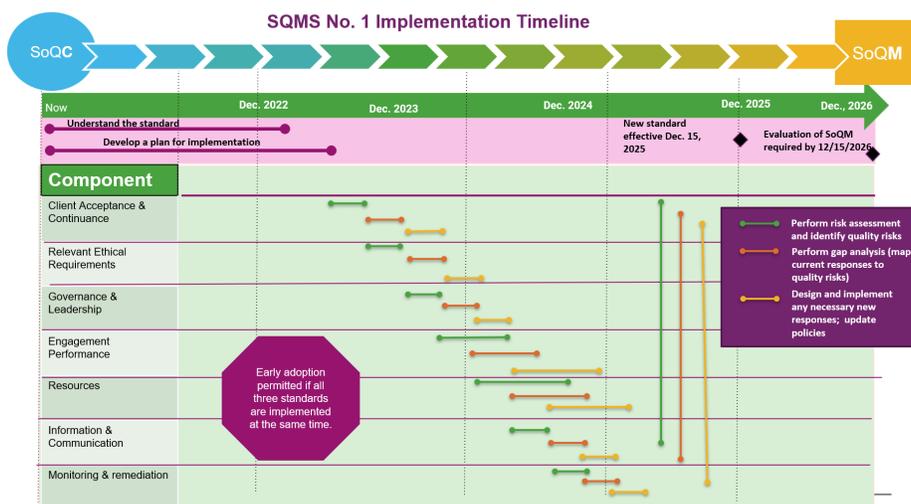
The standards and resources to help you implement the standards can be found [here](#).

Commented [AG1]: To be provided when available.

Appendix: Example timelines of implementation

Timeline Example 1:

This example shows a phased approach to implementing the QM standards by considering one component at a time, and then at the end reconsidering the risk assessment, gap analysis, and responses to quality risks.



Example 2 Timeline:

This timeline demonstrates that the timing of a firm’s peer review does not change the implementation timeline. Beginning in 2022 allows sufficient time to implement prior to the effective date of the standards.

Example Firm Scenarios:	2022	2023	2024	2025	2026
Firm A – Peer review during 2022 and 2026	<ul style="list-style-type: none"> Understand the standards 	<ul style="list-style-type: none"> Perform risk assessment, 	<ul style="list-style-type: none"> Continue risk assessment, gap 	<ul style="list-style-type: none"> Document the SQM 	

Agenda Item 2I – QM Crosswalk

Firm B – Peer review during 2023 and 2027 Firm C – Peer review during 2024 and 2028 Firm D – Peer review during 2025 and 2029	<ul style="list-style-type: none"> • Develop a plan for implementation • Consider quality objectives and if you need to create others 	one component at a time <ul style="list-style-type: none"> • Perform gap analysis, one component at a time • As each component is completed, revisit prior components • Design and implement new responses for those risks that are not addressed • At various points in the process, provide an update to your peer reviewer 	analysis, and design and implementation of new responses until all components have been addressed <ul style="list-style-type: none"> • Review risk assessment and gap analysis at the overall system level and consider if any additional responses are needed 	<ul style="list-style-type: none"> • Determine process for ongoing monitoring (adjusting for changes) and remediation • Understand how to perform root cause analysis • Pre-effective date – implement new processes (on a test basis) and evaluate, adjust as necessary • Fully implement SQMS 1 by December 15, 2025 • At various points in the process, provide an update to your peer reviewer 	<ul style="list-style-type: none"> • Operate SQM in accordance with SQMS 1 • Evaluate system of quality management by December 15, 2026
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Tips:

- No matter when a firm’s peer review occurs, don’t delay starting the implementation of the QM standards! December 2025 may seem a long ways off, but starting now will provide sufficient time for a smooth and successful transition of your quality control system to your quality management system. Delaying your implementation efforts is not advisable!
- Peer review is performed based on standards in effect or early adopted by the firm. For system reviews before December 15, 2025, the peer review would be based on QC section 10 (unless the firm has fully adopted SQMS 1). A phased approach to implementation does not mean SQMS 1 has been fully adopted; rather, it is only after all phases are complete that a firm would determine that SQMS 1 has been fully adopted.
- You may find it helpful to consult with your peer reviewer at various points in the process: when you develop your implementation plan; after your first “round” of risk assessment and gap analysis; when you begin to design and implement responses; and in deciding the nature and extent of documentation of your SQM. Remember that your peer reviewer, to maintain independence, cannot be part of your system of quality management (just like you can’t be part of your client’s system of internal control over financial reporting) but can advise you.

Executive Summary

Overview

The Auditing Standards Board (ASB) has issued the following standards (collectively, the QM standards):

- Statement on Quality Management Standards (SQMS) No. 1, *A Firm's System of Quality Management*
- SQMS No. 2, *Engagement Quality Reviews*
- Statement on Auditing Standards No. 146, *Quality Management for an Engagement Conducted in Accordance With Generally Accepted Auditing Standards*

SQMS No.1 supersedes Statement on Quality Control Standards (SQCS) No. 8, *A Firm's System of Quality Control* (QC section 10), and SAS No. 146 supersedes SAS No. 122, *Statements on Auditing Standards: Clarification and Recodification*, as amended, section 220, *Quality Control for an Engagement Conducted in Accordance With Generally Accepted Auditing Standards* (AU-C section 220).¹

The biggest change is the introduction of a risk-based approach to achieving quality objectives, which helps identify and address risks specific to their practice, and creates a more scalable approach to quality for all firms.

The QM standards, among other things, do the following:

- Increase firm leadership responsibilities and accountability, and improve firm governance
- Introduce a risk-based approach focused on achieving quality objectives
- Address technology, networks, and the use of external service providers
- Increase focus on the continual flow of information and appropriate communication internally and externally
- Promote proactive monitoring of quality management systems and timely and effective remediation of deficiencies
- Clarify and strengthen requirements for a more robust engagement quality review (EQR)
- Enhance the engagement partner's (EP's) responsibility for audit engagement leadership and audit quality

¹ All QC and AU-C sections can be found in AICPA *Professional Standards*.

Effective Date

- Systems of quality management in compliance with SQMS No. 1 are required to be designed and implemented by December 15, 2025, and the evaluation of such² is required to be performed within one year following December 15, 2025.
- SQMS No. 2 is effective for
 - a. audits or reviews of financial statements for periods beginning on or after December 15, 2025, and
 - b. other engagements in the firm’s accounting and auditing practice beginning on or after December 15, 2025. An engagement in the firm’s accounting and auditing practice begins when an engagement letter or other agreement to perform attest services is signed, or when the firm begins to perform the engagement, whichever is earlier.³
- SAS No. 146 is effective for engagements conducted in accordance with generally accepted auditing standards for periods beginning on or after December 15, 2025.

Introduction

This executive summary provides an overview of the QM standards.

Background

The development of the standards has been influenced by concerns about audit quality, as indicated by the results of peer reviews and studies by other regulators, such as the following:

- Risks to audit quality correlated with audits, reviews, and attestation engagements performed by EPs who perform a low volume of such engagements
- Consistency issues in the performance of engagements and a lack of focus on planning
- Over-reliance on intellectual resources, such as third-party quality control materials, that are not sufficiently tailored to the nature and circumstances of the firm
- Challenges experienced by smaller firms in applying the standards
- A need to improve firm governance and leadership and the culture and tone at the top of the firm

² See paragraphs 54–55 of SQMS No. 1.

³ See ET section 0.400.39 of the AICPA Code of Professional Conduct. All ET sections can be found in AICPA *Professional Standards*.

The ASB has a strategic objective to converge with the standards of the International Auditing and Assurance Standards Board (IAASB). Accordingly, SQMS Nos. 1 and 2 and SAS No. 146 were developed using International Standard on Quality Management (ISQM) 1, *Quality Management for Firms That Perform Audits or Reviews of Financial Statements, or Other Assurance or Related Services Engagements*; ISQM 2, *Engagement Quality Reviews*, and International Standard on Auditing 220 (Revised), *Engagement Quality Management for an Audit of Financial Statements*, respectively, as the base starting point. The ASB took into consideration that the PCAOB issued Concept Release in December 2019 that considers using ISQM 1 as a starting point for a future PCAOB standard.

In converging, the ASB has used the terms *quality management* and *engagement quality review*, instead of the terms *quality control* and *engagement quality control review*, respectively, used in its current standards. In addition, “Statements on Quality Control Standards” have been retitled “Statements on Quality Management Standards.” These changes were made to reflect the new quality management approach for the firm’s system of quality management in SQMS No. 1, as described in the “Fundamental Aspects of the Standards” section that follows.

Fundamental Aspects of the Standards

SQMS No. 1

A New Approach Focused on Quality Management

The standard takes a new approach that emphasizes the responsibility of firm leadership for proactively managing quality, while at the same time being scalable to deal with differences in the size of firms and nature of the services they provide. The essence of the new approach is to focus firms’ attention on risks that may have an impact on engagement quality. Unlike extant QC section 10, the new approach requires a firm to customize the design, implementation, and operation of its system of quality management (SQM) based on the nature and circumstances of the firm and the engagements it performs. The standard takes a proactive approach to quality management, with an increased emphasis on a continual flow of remediation and improvement.

The Components of the SQM

A SQM addresses the following eight components:

1. The firm’s risk assessment process (new)
2. Governance and leadership (adapted from the leadership responsibilities for quality within the firm component in QC section 10)
3. Relevant ethical requirements (same name as component in QC section 10)
4. Acceptance and continuance of client relationships and specific engagements (same name as component in QC section 10)

5. Engagement performance (same name as component in QC section 10)
6. Resources (adapted from the human resources component in QC section 10)
7. Information and communication (new)
8. The monitoring and remediation process (adapted from the monitoring component in QC section 10)

As indicated by illustration 1, the components are highly integrated and do not operate in a linear manner.

Illustration 1: The components of an SQM



Objective of the Standard

The objective of the standard includes both the *objective of the firm* and the *objective of the SQM*. The *objective of the firm* in the context of the standard is to design, implement, and operate a *SQM* that provides the firm with reasonable assurance that the *objectives of the SQM* are achieved. The *SQM* is designed to achieve the following two objectives:

- a. The firm and its personnel fulfill their responsibilities in accordance with professional standards and applicable legal and regulatory requirements, and conduct engagements in accordance with such standards and requirements.
- b. Engagement reports issued by the firm are appropriate in the circumstances.

An effective SQM provides the firm with reasonable assurance regarding the achievement of the two objectives. In this context, reasonable assurance is not intended to be obtained through independent assurance that the system is effective (that is, for example, by having a peer review every year), but rather it is obtained through the operation of the system as a whole.

Risk Assessment Process

SQMS No. 1 includes a new approach that focuses firms' attention on risks that may have an impact on engagement quality. The firm's risk assessment process is a new component that comprises the process the firm is required to follow in implementing the risk-based approach to quality management.

The risk assessment is a three-step process:

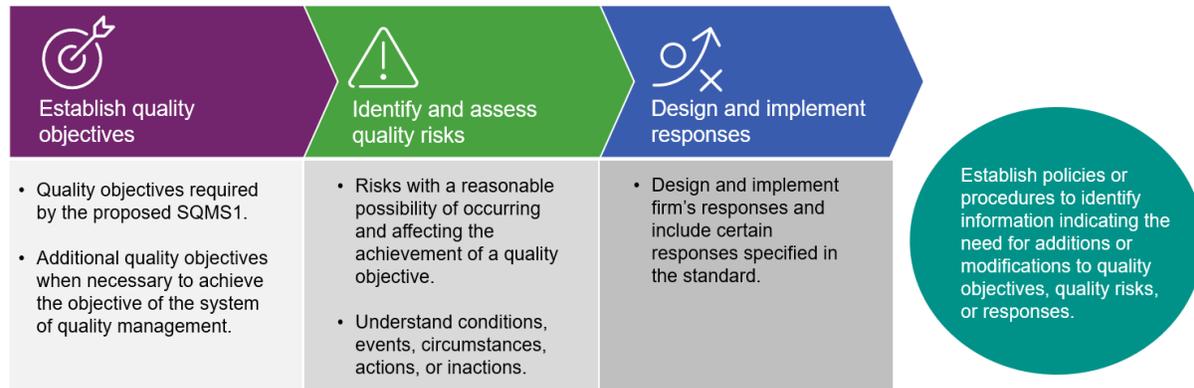
1. *Establish quality objectives.* The standard requires the firm to establish specific quality objectives, based on the nature and circumstances of the firm and its engagements, for each component except risk assessment and monitoring and remediation. The firm is required to establish additional quality objectives when necessary to achieve the objective of the SQM; however, the firm may not find it necessary to establish additional quality objectives.
2. *Identify and assess risks to the achievement of the quality objectives* (referred to in the standard as *quality risks*). Identifying and assessing quality risks involves:
 - a. understanding the factors (that is, the conditions, events, circumstances, actions, or inactions) that may adversely affect the achievement of the quality objectives, and
 - b. identifying and assessing the quality risks by taking into account how and the degree to which the factors may adversely affect the achievement of the quality objectives. (The assessment of identified quality risks does not require formal ratings or scores.)

A risk arises from how, and the degree to which, a condition, event, circumstance, action, or inaction may adversely affect the achievement of a quality objective. Not all risks meet the definition of a *quality risk*.

3. *Design and implement responses to address the quality risks.* The nature, timing, and extent of the firm's responses to address the quality risks are based on, and responsive to, the reasons for the assessments given to the quality risks. Certain responses are specified in the standard; however, the specific responses required by the standard will not be sufficient for the firm to address all its quality risks.

Firms are also required to identify information indicating the need for additions or modifications to quality objectives, quality risks, or responses.

The risk assessment process



Governance and Leadership

SQMS No. 1 provides substantial enhancements to improve the robustness of firms' governance and leadership. In particular, it addresses the expected behavior of firm leadership in setting the tone at the top, the appropriate qualifications of leadership, and holding leadership accountable through performance evaluations. The standard also now addresses the importance of quality in the firm's strategic decisions and actions, including financial and operational priorities, as well as firm leadership's ability to influence decisions about the firm's resources.

The firm is required to assign ultimate responsibility and accountability for the SQM to the firm's CEO, managing partner (or equivalent) or, if appropriate, managing board of partners (or equivalent). In addition, the firm is required to assign the following to designated individuals:

- Operational responsibility for the SQM
- Operational responsibility for specific aspects of the SQM, including compliance with independence requirements and the monitoring and remediation process

Resources

Extant QC section 10 addresses only human resources. SQMS No. 1 expands this to address all resources that the firm needs both to operate the system and to perform engagements. These resources cover:

- technological resources, for example, audit tools or IT applications used by the firm for independence monitoring;
- intellectual resources, for example, the firm's methodology, guidance, templates, or tools; and

- human resources, which may include people outside the firm used in engagements, including component auditors or EQR reviewers who are external to the firm.

The standard focuses on what resources are needed, how they are used and maintained, and whether they are appropriate. The principles-based nature of the requirements relating to resources take into account the variety of resources used and their source. SQMS No. 1 also covers the use of resources from service providers and how to determine that those resources are appropriate for the intended use by the firm. A resource from a service provider could be a methodology, an IT application or people used in an engagement. Services that come from a firm's network, if the firm belongs to a network, are not considered as coming from a service provider (see the section "Network" that follows).

Information and Communication

SQMS No. 1 includes a new component, information and communication. The new component underscores the importance of a continuous flow of information and communication by linking the exchange of information to the firm's culture, so that it is driven from top leadership throughout the firm. The standard requires that the firm establish an information system with processes to identify, capture, process, and maintain information, acknowledging that less complex firms with fewer personnel and direct involvement of leadership may accomplish the objective with less rigorous or detailed policies and procedures.

Both internal and external communication are dealt with in the standard. From an internal perspective, it reinforces the need for robust communication throughout the firm. From an external perspective, the standard reinforces a key public interest issue, which is encouraging firms to be transparent to external parties about their SQM in a relevant, innovative, and proactive manner. In order to drive the proactivity of communication, the standard requires firms to establish policies and procedures that address when communications with external parties are appropriate. In order to promote continual innovation in this area, the standard provides flexibility regarding the specific information communicated, the form of that communication, and the nature, timing, and extent of communication.

Monitoring and Remediation

SQMS No. 1 enhances monitoring activities and shifts the focus from engagement level monitoring to monitoring the entire SQM. The standard promotes more proactive and effective monitoring activities through increased emphasis on tailoring the monitoring activities sufficient to provide a basis for the firm to evaluate the SQM.

The new requirements emphasize factors that firms should consider in designing monitoring activities, rather than prescribing such activities. The nature, timing, and extent of monitoring activities will be driven many firm specific factors, including the following:

- How the underlying system is designed
- The nature and circumstances of the firm and engagements it performs

- The extent of changes to the system
- The results of previous monitoring activities or external inspections

The standard includes a requirement to inspect completed engagements and for EPs to be inspected on a cyclical basis. The firm determines its inspection criteria, including how often to select completed engagements, which completed engagements to select, which EPs to select, and how frequently to select an EP, taking into account factors such as other types of monitoring the firm does, areas of risk, and how the system is designed.

The standard includes requirements for evaluating findings, identifying deficiencies, and evaluating the severity and persuasiveness of the deficiencies. These include a new requirement to investigate the root cause of identified deficiencies. The requirement is intended to be flexible to encourage firms to scale the nature, timing, and extent of the procedures to investigate the root cause of the deficiencies so that they are appropriate and tailored to the circumstances. The evaluation of the severity and pervasiveness of deficiencies is also used by leadership in evaluating the system and concluding whether it achieved its objectives.

A number of improvements were also made to address remediation, including requirements of leadership to assure that remedial actions have been implemented and are effective.

Networks

SQMS No. 1 requires that if a firm is subject to network requirements or uses network services, the firm should understand how those requirements or services fit into the firm's SQM and determine whether the requirement or service needs to be adapted or supplemented to be appropriate for use in the firm's SQM. The standard addresses monitoring activities undertaken by the network and requires the firm to determine the effect of network-level monitoring activities on the firm's monitoring activities. The firm is also required to understand the overall scope of the monitoring activities undertaken by the network across the network firms, including monitoring activities to determine that network requirements have been appropriately implemented across the network firms and to obtain information annually about the results of the network's monitoring activities. This is intended to drive improvements at the network level because firms will need networks to provide more information than they may be providing now.

Scalability

The new quality management approach drives a firm to think about the nature and circumstances of the firm and the engagements it performs in designing, implementing, and operating its SQM, and the approach is focused on achieving quality objectives that are outcome-based. Although this approach is expected to generate multiple benefits for engagement quality, one of the most important benefits is a tailored SQM that is suitable for the nature and circumstances of the firm and the engagements it performs. Thus, this approach is inherently scalable for firms of different sizes and complexity.

SQMS No. 2

Relationship Between SQMS No. 2 and SQMS No. 1

SQMS No. 1 requires that the firm determine when an EQR is an appropriate response to quality risks. SQMS No. 2 contains requirements for policies and procedures addressing the appointment and eligibility of EQR reviewers and performance of EQRs. Although there will no longer be requirements for the performance of EQRs in AU-C section 220, SAS No. 146 contains requirements regarding the EP's responsibilities relating to the EQR, which largely focus on how the EP and the engagement team interact with the EQR reviewer.

Why a Separate Standard?

The requirements for EQRs currently reside in extant QC section 10⁴ and AU-C section 220.⁵ Having a separate standard for EQRs is expected to provide a number of benefits, including the following:

- Clarifying that an EQR can be a response to quality risks for any type of engagement, not only audit engagements
- Placing emphasis on the importance of the EQR
- Facilitating the enhancement of the robustness of the requirements for the eligibility of EQR reviewers and the performance and documentation of the EQR
- Providing a mechanism to more clearly differentiate the responsibilities of the firm and the EQR reviewer
- Increasing the scalability of SQMS No. 1 by not including requirements that would be irrelevant in circumstances when a firm determines that there are no engagements for which an EQR is an appropriate response to address the quality risks

Objective of the Standard

The objectives of the ASB's standards describe the desired outcome of applying the requirements in the standard. Accordingly, the objective of SQMS No. 2 reflects the intended outcome, which is the performance of an objective review of the engagement team's significant judgments and the conclusions reached thereon (that is, an EQR).

⁴ Paragraphs .38–.48 of QC section 10, *A Firm's System of Quality Control*.

⁵ Paragraphs .21–.22 of AU-C section 220, *Quality Control for an Engagement Conducted in Accordance With Generally Accepted Auditing Standards*.

Appointment and Eligibility of Reviewers

The requirements in SQMS No. 2 for the appointment and eligibility of the EQR reviewer (whether internal to the firm or external) are more robust than those in extant QC section 10. Requirements and application material have been added to address the following:

- The eligibility of the individuals within the firm responsible for the appointment of EQR reviewers
- The eligibility of individuals to assist the EQR reviewer in performing the EQR
- The authority, competence, and capabilities of the EQR reviewer, including sufficient time to perform the EQR,
- The EQR reviewer taking responsibility for the performance of the EQR, including that the work of individuals assisting in the EQR is appropriate

The requirements also address compliance with relevant ethical requirements, including that threats to objectivity of the EQR reviewer are eliminated or reduced to an acceptable level.

Performance and Documentation of the EQR

Significant Judgments and Significant Matters

The requirements for the performance of the EQR focus the EQR reviewer's attention on significant judgments and significant matters. The standard includes a stand-back requirement for the EQR reviewer to determine whether the performance requirements of the SQMS with respect to the performance of the EQR have been fulfilled. Once the EQR reviewer has made this determination, the EQR reviewer is required to inform the EP that the EQR is complete.

Timing of the Review

An effective EQR is achieved when the EQRR is involved at appropriate points in the engagement, consistent with when significant judgments are being made by the engagement team because doing so facilitates the resolution of issues in a timely manner. Accordingly, SQMS No. 2 includes a new requirement addressing the EQR reviewer's responsibility to perform the procedures at appropriate points in time during the engagement.

Documentation

SQMS No. 2 includes a specific requirement for the EQR reviewer to take responsibility for documentation of the EQR and adds a requirement that the documentation be filed with the engagement documentation. The standard also includes an overarching requirement for the documentation to be sufficient to enable an experienced practitioner, having no previous

connection to the engagement, to understand the nature, timing, and extent of the EQR procedures performed.

SAS No. 146

Overall Matters

The public interest is served by the consistent performance of quality engagements. SAS No. 146 addresses public interest considerations by encouraging proactive management of quality at the engagement level, emphasizing the importance of the exercise of professional skepticism, enhancing the documentation of the auditor's judgments, and reinforcing the need for robust communications during the audit.

SAS No. 146 addresses how the EP leverages the firm's system and manages quality at the engagement level. The SAS makes clear that the EP has overall responsibility for managing and achieving quality. This includes creating an environment that emphasizes the firm's culture and expected behavior of engagement team members. These behaviors include the responsibility of all engagement team members for quality; the importance of professional ethics, values, and attitudes; and the importance of professional skepticism to a quality audit.

The EP remains ultimately responsible and, therefore, accountable, for compliance with the requirements of the SAS. The phrase *take responsibility for...* is used for those requirements for which the EP is permitted to assign the design or performance of procedures, tasks, or actions to appropriately skilled or suitably experienced members of the engagement team. For other requirements, the SAS expressly intends that the requirement or responsibility be fulfilled by the EP. To fulfill the requirement, the EP may obtain information from the firm or other members of the engagement team, (for example, information to make the required decision or judgment).

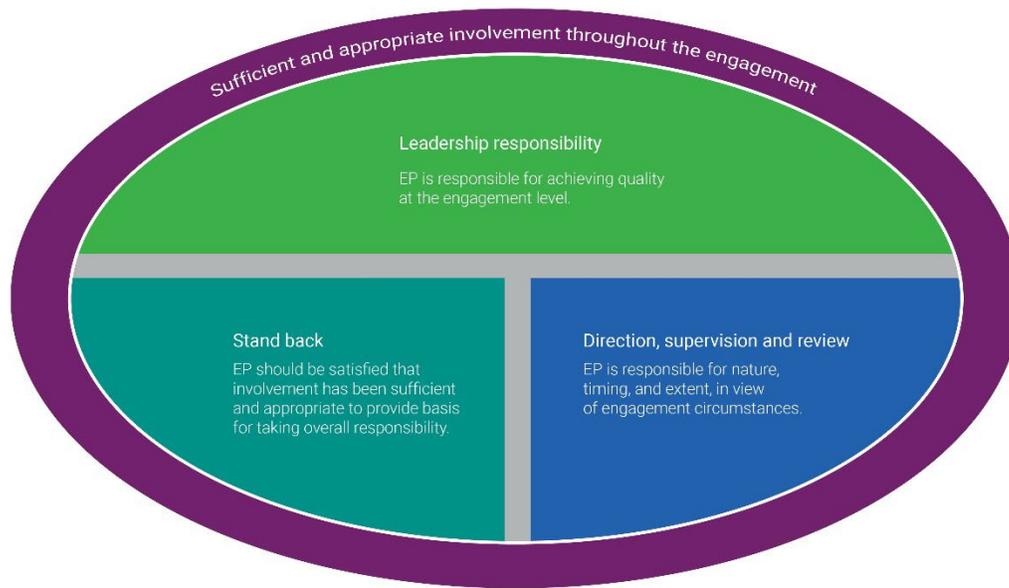
Ordinarily, the engagement team may depend on the firm's policies or procedures in complying with the requirements of this SAS, unless the engagement team's understanding or practical experience indicates that the firm's responses to quality risks are ineffective in context of the specific engagement or information provided by the firm or other parties indicates that the firm's policies or procedures are not operating effectively.

EP's Overall Responsibility for Managing Quality on Audits, Including Engagement Performance and Stand Back

The EP needs to be sufficiently and appropriately involved throughout the engagement as this is fundamental to providing the engagement leadership required to achieve high quality audits and, therefore, to meeting the objective of SAS No. 146. The following diagram illustrates the EP's overall responsibility to manage and achieve quality on the engagement and how it is demonstrated through sufficient and appropriate involvement throughout the engagement, such

that the significant judgments made and the conclusions reached are appropriate given the nature and circumstances of the audit.

The engagement partner’s overall responsibility



Group Audit Engagements

Engagement team members in a group audit engagement may include personnel who are external to the firm (for example, engagement team members who are from network firms or are service providers, such as component auditors from firms not within the firm’s network). AU-C section 600, *Special Considerations — Audits of Group Financial Statements (Including the Work of Component Auditors)*, deals with special considerations that apply to an audit of group financial statements, including when component auditors are involved. Application guidance in SAS No. 146 states that the firm or EP may take different actions with respect to component auditors or other personnel who are external to the firm than the actions applicable to firm personnel. Additionally, examples are included in application guidance in SAS No. 146 of considerations that may be made when component auditors are members of the engagement team.⁶ Conforming amendments to AU-C section 300, *Planning an Audit*, clarify in paragraph .09 that the audit plan should include a description of the nature, timing, and extent of the planned direction and supervision of engagement team members and the review of their work. This includes engagement team members who are external to the firm, such as component auditors.

⁶ See paragraphs A24, A25, A38, A54, A60, A76, A80, A91, A92, and A107 of SAS No. 147.

Relevant Ethical Requirements

In addition to enhancing the extant requirements, SAS No. 146 includes requirements regarding the following:

- Understanding of the relevant ethical requirements and whether other members of the engagement team are aware of those requirements and the firm’s related policies or procedures
- Threats to compliance with relevant ethical requirements
- Determining whether relevant ethical requirements, including those related to independence, have been fulfilled

SAS No. 146 also includes new application material that links with the firm-level requirements in SQMS No. 1, describes possible appropriate actions if noncompliance is indicated, and links to the requirement in AU-C section 700, *Forming an Opinion and Reporting on Financial Statements*,⁷ for the auditor’s report to include a statement regarding the auditor’s independence.

Engagement Resources

The EP is required to take responsibility for the direction and supervision of the engagement team and review of their work. This includes tailoring the nature, timing, and extent of this responsibility to the nature and circumstances of the engagement and the resources — technological, intellectual, and human — assigned to the engagement. If the resources are insufficient or inappropriate, the EP is required to take appropriate action.

Other New Requirements

The SAS clarifies what the EP needs to review, which are significant matters and significant judgments, and formal written communications to management and those charged with governance.

⁷ Paragraph .28c of AU-C section 700, *Forming an Opinion and Reporting on Financial Statements*.

Fraud – Cover Memo

I. Objective of Agenda Item

To inform the ASB about recent activities of the IAASB fraud project and to obtain preliminary feedback from the ASB on certain matters.

II. Fraud Task Force

The Fraud Task Force (the TF) members are:

Tania Sergott, <i>Chair</i>	Barbara Andrews (AICPA - Forensics)
Maxene Bardwell	Patricia Bottomly
Jeanne Dee	Heather Funsch
Diane Hardesty	Bob Harris
Chris Rogers	

The task force is staffed by Linda Delahanty.

III. Background

In December 2021, the IAASB approved the fraud project proposal, *Revision of ISA 240 and the Conforming and Consequential Amendments to Other Relevant ISAs to Enhance or Clarify the Auditor's Responsibilities on Fraud in an Audit of Financial Statements*.

The IAASB fraud task force has divided the issues and proposed actions included in the project proposal into digestible pieces for discussion at upcoming meetings and covered the following topics at the March 2022 IAASB meeting:

1. Identifying and assessing the risks of material misstatement due to fraud
2. Communication with those charged with governance
3. Transparency in reporting
4. Developing nonauthoritative guidance for ISA 240

Ms. Sergott will provide the ASB with an overview of the IAASB project plan and an update from discussion held at the March 2022 IAASB meeting. She will also ask ASB members if they have any comments on the possible actions or direction the IAASB is taking with their Fraud project. See agenda item 3A.

V. Agenda Items Presented

- **Item 3** Fraud Cover Memo
- **Item 3A** Summary of the IAASB's fraud project (for complete IAASB project proposal [click here](#) or on the link provided in the next section)

For Informational/Reference Purposes

- **Item 3B** ASB Comment Letter to the IAASB dated January 29, 2021
- [\[Click here to view\]](#) IAASB Project Proposal, *Revision of ISA 240 and the Conforming and Consequential Amendments to Other Relevant ISAs to Enhance or Clarify the Auditor's Responsibilities on Fraud in an Audit of Financial Statements*
- [\[Click here to view\]](#) March 2022 IAASB PowerPoint presentation during Fraud discussion

Ms. Sergott will use agenda item 3A in leading the discussion.

Agenda Item 3 – Fraud

Agenda item 3B and reference links have been provided for informational purposes only and will not be discussed during the ASB meeting.

ASB Meeting – May 11-12, 2022

Agenda Item 3A – Fraud



IAASB Fraud Project Timeline

Aug 2020:

Issued Discussion Paper

Jan 2021:

Comments due on Discussion Paper

Apr/Jun/Jul 2021:

Discussed comments and proposals

Dec 2021:

Approved Project Proposal

March 2022:

Request input on specific proposed actions to address three issues:

- Risk identification and assessment
- Communication with those charged with governance
- Transparency
- Non-authoritative guidance

IAASB Task Force Members:

- Lyn Provost – New Zealand, former Controller and Auditor General of NZ
- Julie Corden – Canada, Deloitte
- Josephine Jackson – UK, FRC
- Len Jui – Hong Kong, KPMG
- Diane Larsen – US, E&Y

JUNE 2022

Intro, definitions, JE requirements, specialized skills, presumed fraud risk (revenue recognition)

Jun 2023:

Issue exposure draft

Oct 2023:

Comments due on exposure draft

Dec 2024:

Issue final standard

March 2022 IAASB Topics of Discussion

Identifying and Assessing Risks:

- Restructure 240 to align with order of 315R
- Develop AM to clarify that risk assessment procedures in 240 are not separate from those in 315R
- Make revisions to “inquiries of mgmt and TCWG”
- Consider “sources of other info” with a fraud lens (acceptance & continuance, 720 procedures, other procedures)
- Make the engagement team discussion more robust
- Emphasize the importance of UEE on the consideration of fraud
- Include a stronger link to the susceptibility to misstatement in applying the financial reporting framework
- Reflect a “fraud lens” for understanding each of the components of the system of internal control
- Split the requirements for identifying RoMMs and assessing RoMMs
- Keep list of fraud risks factors as an appendix, but incorporate into examples within the AM, and modernize list

Communication with Those Charged With Governance

- Specifically communicate assessment of RoMMs due to fraud
- Two-way discussion about specific fraud-related matters, including consideration of who to talk to and who to assign from the audit team
- Ongoing communications – new requirement or new AM??
- Inquiries of TCWG are in part to corroborate inquiries with mgmt
- New requirement to determine whether remediation measures (for identified control deficiencies or misstatements due to fraud) are appropriate
- New AM to clarify that effective participation by TCWG is influenced by their independence from management and their ability to objectively evaluate the actions of management

Transparency:

Undertake **targeted outreach to users** of general-purpose financial reports – share examples of fraud disclosures from UK & NL reports and present the alternatives shown below (also ask “what else can be done to clarify auditor’s responsibilities” and “what is the appropriate scope of transparency requirements” (e.g., all entities, PIEs only, listed only)):

1. Detailed description of the fraud risks identified, the auditor’s response, and the auditor’s findings/observations
2. High-level description of the fraud risks identified & how the auditor addressed the fraud risks (*similar to NL*)
3. Explain to what extent the audit is considered capable of identifying & assessing RoMMs due to fraud (*similar to UK*)
4. Mechanism other than the auditor’s report to demonstrate the enhanced transparency that is being called for.
For example, this transparency could include one or more of the following:
 - Emphasizing, using the existing requirements for the communication of KAMs, when there is a RoMM due to fraud
 - Strengthened communication and two-way discussions with TCWG about the RoMMs due to fraud, the auditor’s responses to address the assessed ROMMs, and the findings from those procedures

Non-Authoritative Guidance:

- Higher-level depiction of linkage between 240 and other ISAs
- Holistic diagram, together with a narrative succinctly describing the important linkages between certain standards that underpin ISA 240 (i.e., ISA 200, ISA 315R and ISA 330)
- Detailed depiction of the interrelationships between ISA 240 and the other ISAs is better suited to the end of the project

Outcomes from March 2022 IAASB Meeting

Identifying and Assessing Risks

- Overall, IAASB generally agreed with restructuring 240 to follow 315R, but with some concerns:
 - Changing structure won't change behavior – but could assist with linkage to 315R
 - 240 should not repeat all of 315R, linkage should be targeted instead of duplicative
 - Some commented that fraud risk assessment guidance should be in 315R and not in 240 – but TF will not pursue combining with 315R
- Distinguish “sources of info” in 240 between “other information” in 720
- Keep scalability in mind
- Incorporate “ecosystem” by obtaining management’s fraud risk assessment as a starting point for auditor’s risk assessment

Communication with Those Charged With Governance

- Majority supported a new requirement to supplement the 260 requirement regarding the timing of communication (rather than as application material)
- Emphasize two-way discussion, where those charged with governance comes prepared to talk about the entity’s fraud risk assessment

Transparency

- IAASB supported undertaking targeted outreach to users of general-purpose financial reports

Non-Authoritative Guidance:

- IAASB supported nonauthoritative guidance with comments (define what is meant by fraud lens, make it clear there is more guidance to come) – issue by end of April

Questions for ASB Consideration

1. Does the ASB have any comments about the direction the IAASB may take related to the topics covered in March:

- Identifying and assessing risks
- Communication with those charged with governance
- Transparency in the auditor's report
- Nonauthoritative guidance

June 2022 IAASB
Topics of Discussion

The following topics will be discussed at the June 2022 IAASB meeting:

- Reorganize introductory paragraphs of ISA 240
- Definition of fraud
- Journal entry requirements
- Specialized skills
- Presumed fraud risk (revenue recognition)

Introductory Paragraphs in ISA 240 – Emphasis on the Auditor’s Responsibilities

Enhance and clarify the introductory paragraphs in ISA 240 to emphasize the auditor’s responsibilities regarding fraud, including:

- Considering changes and enhancements made by others in different jurisdictions in their equivalent of ISA 240 to reduce the ambiguity between the inherent limitations of an audit and the auditor’s responsibilities for fraud in an audit of financial statements.
- Considering whether to provide context for the auditor’s responsibilities by explaining the responsibilities of others in the financial reporting ecosystem (relevant to the financial statement audit) within the introductory paragraphs.
- Considering whether the auditor’s responsibilities should be placed prior to the description of inherent limitations of an audit

Application Material – Definition of Fraud

Enhance application material to clarify how concepts such as bribery and corruption, and money laundering, relate to the definition of fraud for purposes of an audit of financial statements, including consideration of the most appropriate standard for this application material (i.e., ISA 240 or ISA 250 (Revised)).

Requirements and Application Material – Journal Entries

Clarify the requirements and application material in ISA 240 on the approach to testing journal entries, including:

- Considering enhancing requirements in ISA 240 to:
 - o Clarify that the auditor's risk assessment procedures performed as part of ISA 315 (Revised 2019) for controls over journal entries are also relevant to the auditor's decisions on journal entry testing in ISA 240.
 - o Take account of the impact of technology when testing journal entries.
 - o Address the extent of testing of journal entries to respond to identified risks.
- Enhancing application material to:
 - o Clarify what the auditor's objectives are when testing journal entries, and explain how auditors may determine the nature, timing and extent of the auditor's procedures for journal entry testing.
 - o Consider the impact of any proposed changes being made to ISA 500 (e.g., obtaining audit evidence about the completeness of the information used to test journal entries).

Requirements and Application Material – Specialized Skills

Consider enhancing requirements and application material in ISA 240 on the need for specialized skills (including forensic skills):

- Consider a new requirement and enhanced application material for those **circumstances when it is appropriate for the auditor to “consider the need for specialized skills, including forensic skills”** to assist with audit procedures, such as:
 - When performing risk identification and assessment. In doing so, consider how this links to the revised requirements in ISA 220 (Revised) for adequate resources for the engagement.
 - When there is identified or suspected fraud.
- Consider how scalability of a new requirement can be achieved by taking into the account the nature and circumstances of auditors to have access to such specialized skills, in particular, auditors of less complex entities (LCEs).
- Consider how to describe “forensic skills,” in light of comments that this term is not commonly understood (i.e., clarify what may qualify as forensic skills).
- Consider changes made by others in different jurisdictions relating to the use of specialized skills

Requirements and Application Material – Presumption of Fraud Risk in Revenue Recognition

Revise requirements and enhance application material in ISA 240 to clarify how performing a robust risk assessment is critical in determining whether or not the presumption of fraud risk in revenue recognition is applicable, including:

- Revising the requirement in ISA 240 to shift the focus from the auditor developing a rebuttal to emphasizing the importance of performing robust risk identification and assessment.
- Enhancing the application material in ISA 240 to:
 - o Highlight other account balances that may be particularly susceptible to material misstatement due to fraud (such as goodwill).
 - o Clarify when it is inappropriate to rebut the presumption of risks of fraud in revenue recognition (shifting away from clarifying when it may be appropriate to rebut the presumption of risk of fraud in revenue recognition).
 - o Describe public sector considerations

Questions for ASB Consideration

1. Does the ASB have any comments about the possible actions the IAASB may take related to the topics to be covered in June:

- Reorganize introductory paragraphs of ISA 240
- Definition of fraud
- Journal entry requirements
- Specialized skills
- Presumed fraud risk (revenue recognition)

Appendix: Summary of Project Proposal

Key Issues Identified During Research Phase

Key Issues Identified that Will be Addressed by the Project on Fraud

a) Role and responsibilities of the auditor on fraud in an audit of financial statements:

- i. The introductory paragraphs in ISA 240 explaining the inherent limitations of an audit can be misleading and result in misunderstanding of the auditor's obligations.
- ii. A need has been expressed to clarify & emphasize the auditor's responsibilities regarding fraud in an audit of f/s.
- iii. There are terms and concepts associated with fraud, such as bribery, corruption, and money laundering, that are not directly addressed in the definition of fraud, and it has been noted that it is therefore unclear whether the auditor's procedures extend to include work related to such terms and concepts.
- iv. Calls for the auditor undertaking more forensic type procedures, or the need for forensic specialists on all, or some, audits have been made due to the increasing use of forensic procedures on audits, including by forensic specialists.

b) Identifying and assessing risks of material misstatement due to fraud:

- i. The auditor's risk identification and assessment process as it relates to fraud should be more robust (many aspects of the enhanced risk identification and assessment procedures in ISA 315R have not been reflected in ISA 240).
- ii. The engagement team discussion is not sufficiently robust with respect to the auditor's considerations of fraud throughout the audit.

****Proposed Actions for RISK ASSESSMENT discussed in March 2022****

Key Issues Identified that Will be Addressed by the Project on Fraud

(c) Responses to the assessed risks of material misstatement due to fraud:

- i. The auditor's responses to the assessed risks of material misstatement due to fraud should be more robust.
- ii. The auditor is inappropriately relying on written representations provided by management addressing fraud in the entity (i.e., clarity is needed that written representations do not relieve the auditor of the responsibility to appropriately respond to the assessed risks of material misstatement due to fraud)

(d) Use of technology:

- (i) ISA 240 needs to consider the impact of the entity's ability to use technology to enable fraudulent activity on the auditor's procedures.
- (ii) ISA 240 needs to be modernized for the auditor's considerations about how new and evolving technologies, and current practice, impacts the auditor's procedures when considering fraud.

(e) Relationship between and linkage of ISA 240 with respect to ISA 250 (Revised)¹⁰ and the other ISAs:

- (i) The relationship between ISA 240 and ISA 250 (Revised) is unclear, i.e., more clarity is needed if a fraud is identified or suspected, whether the auditor is performing procedures to comply with ISA 240 or ISA 250 (Revised).
- (ii) The relationship between ISA 240 and other ISAs (e.g., standards addressing quality management, written representations, and external confirmations) should be clarified to promote an integrated risk-based approach with respect to fraud.

Key Issues Identified that Will be Addressed by the Project on Fraud

(f) Specific fraud-related audit procedures:

- (i) Journal entries – uncertainty about how to select which JEs to test that has resulted in inconsistent application.
- (ii) Presumption of fraud risk in revenue recognition – it is not clear when it may, or may not, be appropriate to rebut the presumption of fraud risk in revenue recognition, which has resulted in inconsistent application.
- (iii) Presumption of fraud risk in other account balances – stakeholders have questioned whether the presumption of fraud risk should be extended to include other account balances, such as goodwill.
- (iv) Analytical procedures – analytical procedures at the planning and completion stages of the audit are not robust enough to support the auditor’s consideration of the risk of fraud and the planned audit response (nature, timing, extent of audit procedures).
- (v) Fraud is identified or suspected – lack of clarity around the auditor’s response in such circumstances.
- (vi) Unpredictability of audit procedures – unclear as to the required actions or types of fraud-related procedures to be undertaken by the auditor.
- (vii) Non-material fraud – clarity is needed with respect to the auditor’s responsibilities and whether more should be done when a possible non-material fraud is identified or suspected.
- (viii) Third party fraud – clarity is needed around the auditor’s actions with respect to third party fraud.
- (ix) Audit documentation – clarity is needed on what needs to be documented for fraud when identifying and assessing the risk of material misstatement, performing audit procedures and concluding.
- (x) External confirmations – clarity is needed as to whether the external confirmation process, as relevant to the auditor’s considerations on fraud, should be more robust.

Key Issues Identified that Will be Addressed by the Project on Fraud

(g) Professional skepticism:

- (i) The appropriate exercise of professional skepticism needs to be reinforced, including reminding the auditor of the importance of remaining alert to conditions that may indicate possible fraud and maintaining professional skepticism throughout the audit.

(h) Transparency on the auditor's fraud-related procedures:

- (i) The required communications with TCWG on fraud considerations may not be sufficiently robust in the current environment, including that such communications relating to fraud matters are not presently explicitly required throughout the audit.
- (ii) (ii) The auditor's report may not be transparent enough about the auditor's fraud-related responsibilities and procedures

****Proposed Actions for TRANSPARENCY discussed in March 2022****

Proposed Actions to Address
Key Issues Identified

ROLES & RESPONSIBILITIES OF
THE AUDITOR

Proposed Actions to Address the Key Issues Identified

Introductory Paragraphs in ISA 240 – Emphasis on the Auditor’s Responsibilities

Enhance and clarify the introductory paragraphs in ISA 240 to emphasize the auditor’s responsibilities regarding fraud, including:

- Considering changes and enhancements made by others in different jurisdictions in their equivalent of ISA 240 to reduce the ambiguity between the inherent limitations of an audit and the auditor’s responsibilities for fraud in an audit of financial statements.
- Considering whether to provide context for the auditor’s responsibilities by explaining the responsibilities of others in the financial reporting ecosystem (relevant to the financial statement audit) within the introductory paragraphs.
- Considering whether the auditor’s responsibilities should be placed prior to the description of inherent limitations of an audit

Application Material – Definition of Fraud

Enhance application material to clarify how concepts such as bribery and corruption, and money laundering, relate to the definition of fraud for purposes of an audit of financial statements, including consideration of the most appropriate standard for this application material (i.e., ISA 240 or ISA 250 (Revised)).

Proposed Actions to Address the Key Issues Identified

Requirements and Application Material – Specialized Skills

Consider enhancing requirements and application material in ISA 240 on the need for specialized skills (including forensic skills):

- Consider a new requirement and enhanced application material for those **circumstances when it is appropriate for the auditor to “consider the need for specialized skills, including forensic skills”** to assist with audit procedures, such as:
 - When performing risk identification and assessment. In doing so, consider how this links to the revised requirements in ISA 220 (Revised) for adequate resources for the engagement.
 - When there is identified or suspected fraud.
- Consider how scalability of a new requirement can be achieved by taking into the account the nature and circumstances of auditors to have access to such specialized skills, in particular, auditors of less complex entities (LCEs).
- Consider how to describe “forensic skills,” in light of comments that this term is not commonly understood (i.e., clarify what may qualify as forensic skills).
- Consider changes made by others in different jurisdictions relating to the use of specialized skills

Proposed Actions to Address Key Issues Identified

RISK ASSESSMENT

Proposed Actions to Address the Key Issues Identified

Requirements and Application Material – Identifying and Assessing Risks of Material

Enhance and clarify requirements and application material in ISA 240 to incorporate recent changes in ISA 315R to make fraud risk identification and assessment more robust, including:

- Developing explicit fraud considerations in risk assessment procedures.
- Clarifying that risk assessment procedures in ISA 240 are not separate from those in ISA 315R.
- Enhancing the requirements to consider information obtained from acceptance and continuance when obtaining an understanding of the entity and its environment, etc.
- Describing the auditor's specific considerations relating to fraud when obtaining an understanding of the entity and its environment, the applicable FRF and the entity's system of i/c in accordance with ISA 315R, with an emphasis on
 - o The entity's corporate culture.
 - o Entity's key performance indicators (KPIs).
 - o Employee performance measures and incentive compensation policies.
 - o The entity's risk assessment process.
 - o Specific control activities to prevent and detect fraud.
 - o Other information, e.g., matters the auditor is aware of based on the performance of procedures in accordance with ISA 720R or the auditor's knowledge obtained throughout the audit
- Updating the fraud risk factors currently included in the Appendix to ISA 240 and considering whether the fraud risk factors should rather form part of the application material.
- Emphasizing in ISA 240 how fraud risk factors influence the identified risks of material misstatement due to fraud at the assertion level, and therefore in designing a more precise response to such a fraud risk.
- Considering examples in ISA 240 to illustrate the scalability of the requirements, for example by providing examples that are more relevant to LCEs.

Proposed Actions to Address the Key Issues Identified

Requirements and Application Material – Engagement Team Discussion

Enhance requirements and application material in ISA 240 to make the engagement team discussion on fraud considerations more robust, including:

- Enhancing requirements to require specific topics to be included during the engagement team discussion.
- Enhancing application material in ISA 240 to explain when it may be beneficial to hold further engagement team discussion(s).
- Enhancing application material in ISA 240 for when it may be beneficial for specialists (including internal or external fraud specialists) to attend engagement team discussion(s)

Requirements and Application Material – Responses to the Assessed Risks of Material Misstatement

Enhance the requirements and application material in ISA 240 to strengthen the auditor's responses to assessed risks of material misstatement due to fraud, as necessary in light of the proposed actions addressing fraud risk identification and assessment and other fraud-related procedures, including:

- Considering a stand-back requirement in ISA 240 to evaluate all relevant audit evidence obtained, whether corroborative or contradictory, and whether sufficient appropriate audit evidence has been obtained in responding to the assessed risks of material misstatement due to fraud.
- Enhancing application material in ISA 240 to encourage emphasis on management bias when considering the appropriateness of accounting estimates from a fraud perspective as well as improving the link to the procedures required in ISA 540R.

Proposed Actions to Address the Key Issues Identified

Requirements and Application Material – Written Representations from Management

Consider enhancing and clarifying the requirements and application material for written representations from management

Application Material – Technology Considerations

Enhance application material in ISA 240 to reflect and describe the use of technology to:

- Enable fraudulent activity (including cybercrime).
- Perform fraud-related procedures by auditors. In doing so, remaining mindful of maintaining a balance of not ‘dating’ the standard by referring to technologies that may change and evolve, and consulting with a technology expert(s) as needed

Introductory Paragraphs and Application Material in ISA 240 – Relationship Between ISA 240 and ISA 250 (Revised), and Other ISAs

Enhance the introductory paragraphs and consider application material in ISA 240 to clarify the relationship between ISA 240 and ISA 250 (Revised), including:

- Highlighting the interrelationship between fraud and non-compliance with laws and regulations (i.e., fraud usually constitutes an illegal act and therefore, also falls under ISA 250 (Revised)).

Enhance, within the standards, the linkages between ISA 240 and the other ISAs with cross-referencing as appropriate.

Proposed Actions to Address the Key Issues Identified

Requirements and Application Material – Journal Entries

Clarify the requirements and application material in ISA 240 on the approach to testing journal entries, including:

- Considering enhancing requirements in ISA 240 to:
 - o Clarify that the auditor's risk assessment procedures performed as part of ISA 315 (Revised 2019) for controls over journal entries are also relevant to the auditor's decisions on journal entry testing in ISA 240.
 - o Take account of the impact of technology when testing journal entries.
 - o Address the extent of testing of journal entries to respond to identified risks.
- Enhancing application material to:
 - o Clarify what the auditor's objectives are when testing journal entries, and explain how auditors may determine the nature, timing and extent of the auditor's procedures for journal entry testing.
 - o Consider the impact of any proposed changes being made to ISA 50018 (e.g., obtaining audit evidence about the completeness of the information used to test journal entries).

Proposed Actions to Address the Key Issues Identified

Requirements and Application Material – Presumption of Fraud Risk in Revenue Recognition

Revise requirements and enhance application material in ISA 240 to clarify how performing a robust risk assessment is critical in determining whether or not the presumption of fraud risk in revenue recognition is applicable, including:

- Revising the requirement in ISA 240 to shift the focus from the auditor developing a rebuttal to emphasizing the importance of performing robust risk identification and assessment.
- Enhancing the application material in ISA 240 to:
 - o Highlight other account balances that may be particularly susceptible to material misstatement due to fraud (such as goodwill).
 - o Clarify when it is inappropriate to rebut the presumption of risks of fraud in revenue recognition (shifting away from clarifying when it may be appropriate to rebut the presumption of risk of fraud in revenue recognition).
 - o Describe public sector considerations

Application Material – Analytical Procedures

Consider enhancing and clarifying the application material in ISA 240 to emphasize the link to ISA 315 (Revised 2019) and ISA 52019 with respect to analytical procedures at the planning and completion stages of the audit and how such procedures can be effectively used to consider the possibility of fraud.

Proposed Actions to Address the Key Issues Identified

Requirements and Application Material – Fraud Is Identified or Suspected

Designate a separate section in ISA 240 for required audit procedures when fraud is identified or suspected, including:

- Developing new requirements, relocating existing requirements, or elevating existing application material to requirements.
- Enhancing application material as needed.

Application Material – Unpredictability of Audit Procedures

Enhance or clarify application material in ISA 240 on how to design unpredictable audit procedures, including providing examples of the types of procedures that can be used by the auditor, and how such procedures can be scalable.

Introductory Paragraphs and Application Material in ISA 240 – Non-Material Fraud

Enhance the introductory paragraphs and consider application material in ISA 240 to describe the auditor's responsibilities when non-material fraud is identified or suspected (e.g., that more work is required to conclude that it is a non-material fraud, taking into account the quantitative and qualitative characteristics of a possible misstatement).

Application Material – Third Party Fraud

Enhance application material in ISA 240 to determine the auditor's actions when third party fraud is identified or suspected that may give rise to risks of material misstatement due to fraud.

Proposed Actions to Address the Key Issues Identified

Requirements and Application Material – Audit Documentation

Consider the need to enhance or expand the specific documentation requirements in ISA 240, and application material, as appropriate, once the other changes within the standard have been developed (as such changes may necessitate new or revised specific documentation requirements and guidance).

Application Material – External Confirmations

Consider enhancing application material in ISA 240 related to fraud considerations for external confirmation procedures (e.g., when considering third party fraud), including:

- Modernizing ISA 240 for current practice and developments in technology, including technology used in practice for external confirmations.
- Considering the impacts of revisions to ISA 500 on ISA 240 with respect to audit evidence obtained from the external confirmation process.
- Revising the existing guidance when there are non-responses.
- Emphasizing the usefulness of external confirmations as an audit procedure when there is a heightened risk of fraud.

Introductory Paragraphs and Application Material in ISA 240 – Non-Material Fraud

Enhance the introductory paragraphs and consider application material in ISA 240 to describe the auditor's responsibilities when non-material fraud is identified or suspected (e.g., that more work is required to conclude that it is a non-material fraud, taking into account the quantitative and qualitative characteristics of a possible misstatement).

Proposed Actions to Address Key Issues Identified

Professional Skepticism

Proposed Actions to Address the Key Issues Identified

Requirements and Application Material – Professional Skepticism

Enhance requirements and application material in ISA 240 to reinforce more robust exercise of professional skepticism when performing procedures related to fraud, including:

- Enhancing requirements and application material in ISA 240 for the auditor to design and perform procedures that is not biased towards obtaining audit evidence that may be corroborative or towards excluding evidence that may be contradictory.
- Explaining the 'ramp up' of procedures when fraud is identified or suspected in the application material.

Proposed Actions to Address
Key Issues Identified

TRANSPARENCY

Proposed Actions to Address the Key Issues Identified

Requirements & Application Material – Transparency in the Required Communications with TCWG & in the Auditor's Report

- *Enhance requirements and application material in ISA 240 to strengthen required communications with TCWG, including:*
 - o Enhancing the requirements in ISA 240 for specific discussions with TCWG about the entity's risks of material misstatement due to fraud and to encourage more appropriate two-way communication. Enhancements could include, for example, explicit discussions about:
 - Susceptibilities to misstatement due to management bias, and corroborating inquiries of management with TCWG.
 - The auditor's evaluation of the entity's components of internal control (when performing risk assessment procedures in accordance with ISA 315R).
 - o Enhancing the requirements in ISA 240 for the auditor to assess whether the remediation measures taken by management and TCWG for identified or suspected fraud are appropriate
 - o Enhancing the requirements in ISA 240 to emphasize the ongoing nature of communications with TCWG about fraud throughout the audit.
 - o Clarifying in the application material of ISA 240 that effective participation by TCWG is influenced by their independence from management and their ability to objectively evaluate the actions of management.
- *Explore revisions to requirements and enhancements to application material to determine the need for more transparency in the auditor's report describing fraud-related matters, and if needed, how this may be done, including:*
 - o Exploring what changes may be needed to better describe the auditor's responsibilities and procedures related to fraud in an audit of financial statements, including:
 - Additional outreach with investor groups as well as other relevant stakeholders about the need for more transparency in the auditor's report, and how this can be done.
 - Consideration of changes made by others in different jurisdictions.
 - o Considering revisions to clarify the interaction of key audit matters and fraud-related matters



January 29, 2021

Mr. Willie Botha
Technical Director
International Auditing and Assurance Standards Board
529 Fifth Avenue
New York, NY 10017

Re: Discussion Paper — *Fraud and Going Concern in an Audit of Financial Statements: Exploring the Differences Between Public Perceptions About the Role of the Auditor and the Auditor's Responsibilities in a Financial Statement Audit*

Dear Mr. Botha:

The American Institute of Certified Public Accountants (AICPA) Auditing Standards Board (ASB) is pleased to respond to the International Auditing and Assurance Standards Board's (IAASB) above referenced Discussion Paper.

The AICPA is the world's largest member association representing the accounting profession, with more than 431,000 members in 143 countries and a history of serving the public interest since 1887. AICPA members represent many areas of practice, including business and industry, public practice, government, education, and consulting. Among other things, the AICPA sets ethical standards for the profession and U.S. auditing standards (generally accepted auditing standards or GAAS); attestation standards (Statements on Standards for Attestation Engagements or SSAEs); and standards for financial statement preparation, compilation, and review engagements (Statements on Standards for Accounting and Review Services or SSARs) for private companies, nonprofit organizations, and federal, state and local governments (nonissuers).

We support the IAASB's efforts, as set forth in the IAASB's Discussion Paper — *Fraud and Going Concern in an Audit of Financial Statements: Exploring the Differences Between Public Perceptions About the Role of the Auditor and the Auditor's Responsibilities in a Financial Statement Audit* (Discussion Paper), to gather perspectives from stakeholders about the role of the auditor in relation to fraud and going concern in an audit of financial statements, and to obtain input on matters about whether the auditing standards relating to fraud and going concern remain fit-for-purpose in the current environment.

In view of the ASB's commitment to converge its standards with those of the IAASB, the ASB is very interested in the direction the IAASB is moving related to these topics. In November 2020, the ASB requested feedback, through a public survey, to the questions in the IAASB's Discussion Paper from a U.S. GAAS perspective. The results of this survey were used to help inform the ASB's response.

We appreciate the opportunity to help inform the IAASB's direction, and in some cases we provide possible direction to the IAASB based on GAAS requirements. In particular, we note that there are incremental requirements in GAAS relating to fraud and going concern that are not included

Mr. Willie Botha
January 29, 2021

in the International Statements on Auditing Standards (ISAs). We provide additional detail on these incremental requirements in the appendix to this letter. We are glad to provide feedback beyond this letter, as needed.

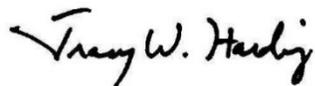
We agree that each participant in the financial reporting ecosystem plays a role that contributes towards high-quality financial reporting, including audit quality, particularly as it relates to fraud and going concern. As an example, we note the importance of an entity's internal control framework as it relates to anti-fraud measures. While we recognize the existence of many internal control frameworks we observe that in the U.S., the 2013 Committee of Sponsoring Organizations of the Treadway Commission (COSO) *Internal Control - Integrated Framework* provides such guidance to many entities.

We encourage the IAASB to continue to develop principles-based standards, without being overly prescriptive considering that these standards may serve as the basis for audits of all entities, whether public or private. We also encourage the IAASB to continue to focus on the "IAASB toolkit." This focus includes the IAASB considering all possible actions that may be taken by the IAASB, beyond making changes to the auditing standards themselves. Further, we encourage the IAASB to continue to share its findings from this project to help inform all stakeholders.

The appendix to this letter provides our more detailed responses to the specific questions presented in the Discussion Paper. Our responses are provided from the perspective of an audit of financial statements of a nonissuer in the United States of America because that is within the purview of the ASB.

Thank you for the opportunity to present our views on the Discussion Paper. If you have any questions regarding the comments in this letter, please contact me at Tharding@berrydunn.com or Linda Delahanty at Linda.Delahanty@aicpa-cima.com.

Respectfully submitted,



/s/ Tracy Harding
Chair, Auditing Standards Board

Appendix

Responses to Questions in the Discussion Paper — *Fraud and Going Concern in and Audit of Financial Statements: Exploring the Differences Between Public Perceptions About the Role of the Auditor and the Auditor’s Responsibilities in a Financial Statement Audit*

Overall Considerations

As noted in our cover letter, we support the IAASB’s efforts to gather perspectives from stakeholders about the role of the auditor in relation to fraud and going concern in an audit of financial statements. Determining whether additional actions may be necessary to enhance the reliability of financial reporting, including audit quality, involves all members of the financial reporting ecosystem, including the financial reporting standard setters, management, those charged with governance and the auditor. Furthermore, we encourage the IAASB to consider various ways in which it may respond to the challenges outlined in the Discussion Paper beyond setting new standards, including non-authoritative guidance and education, and outreach with other members of the ecosystem.

We also note that the users of the auditors’ reports for nonissuers in the U.S. typically have ready access to management and owners. Therefore, such users may have a broader range of information available to them beyond the financial statements, that may not be available to the users of the financial statements of issuers (listed entities). Accordingly, for nonissuers (non-listed entities) there may be less need for information to be communicated through the financial statements and the auditor’s report, and more need for education regarding the nature of an audit and financial information not in the purview of the auditor.

IAASB Question 1(a): In regard to the expectation gap, what do you think is the main cause of the expectation gap relating to fraud and going concern in an audit of financial statements?

Response: We support the IAASB’s effort to assess what is meant by the expectation gap relating to fraud and the expectation gap relating to going concern and applaud their efforts to obtain feedback from stakeholders. We encourage the IAASB to continue to explore the causes of such expectation gaps to inform possible improvements to audit quality. We agree that the differences between what the public thinks auditors do and what auditors actually do, or the “knowledge gap” as described in the Discussion Paper, likely contributes to the expectation gap and believe it may be best addressed through education of the users of the auditor’s report. We note that in some instances auditors may not properly implement the requirements in the auditing standards, however we believe further outreach and research are warranted to assess the extent to which that is a function of the standards being overly complex or unclear, or of auditors not exercising due professional care in interpreting or adhering to the requirements. Such outreach and research would inform decisions regarding allocation of resources to enhance auditor education and instruction and standard setting. A better understanding of the causes of an expectation gap will be helpful to determining what actions will be most effective in reducing the gap.

IAASB Question 1(b): In regard to the expectation gap, in your view, what could be done, by the IAASB and/or others (please specify), to narrow the expectation gap related to fraud and going concern in an audit of financial statements?

Response: We recommend the IAASB consider various options available to address factors contributing to the expectation gap that the IAASB identifies. Users of the financial statements are looking for more insight about the entity, and providing such information, for example, disclosures relating to going concern, begins first with management and those charged with governance. Therefore, further education to users around management’s responsibilities might be helpful. Also, post-implementation reviews, including those related to ISA 315 (Revised 2019), *Identifying and Assessing the Risks of Material Misstatement*, and ISA 540 (Revised), *Auditing Accounting Estimates and Related Disclosures*, are likely to be helpful to aid in identifying areas in the auditing standards that may not be implemented as intended and may need further clarification for the auditor. This type of action may be helpful in decreasing elements of the expectation gap.

Stakeholder Perspective Question (page 15 of the Discussion Paper): The IAASB is interested in perspectives about the impact of corporate culture on fraudulent financial reporting and what, if any, additional audit procedures for the auditor should be considered by the IAASB in this regard.

Response: As noted in the Discussion Paper, there are a variety of sources that recognize that corporate culture is important as it relates to fraudulent financial reporting. We note that corporate culture is considered by the auditor as he or she gains an understanding of the entity, including the entity’s control environment. For example, paragraph 4 of ISA 315 (Revised 2019) states that “the control environment sets the tone of an organization, influencing the control consciousness of its people, and provides the overall foundation for the operation of the other components of the entity’s system of internal control.” Internal control frameworks, such as COSO, also recognize the importance of corporate culture as part of an effective control environment that can help to deter fraud. The consideration of corporate culture as part of risk assessment affects the auditor’s professional skepticism and professional judgment and influences the audit work needed.

We recognize that corporate culture may be preliminarily considered, to some degree, as part of the client acceptance and continuance process. Accordingly, we recommend the IAASB reflect on whether additional guidance (for example, application material, staff guidance or case studies) should be developed about inquiries being performed as part of client acceptance and continuance decisions (in addition to during risk assessment procedures) relating to the tone at the top, including corporate culture and how the results of those inquiries later inform the auditor’s risk assessment.

IAASB Question 2(a): In your view, should the auditor have enhanced or more requirements with regard to fraud in an audit of financial statements? If yes, in what areas?

Response: National Standard Setters have developed guidance incremental to what is in the ISAs that the IAASB might find helpful. For example, in GAAS, various sections from ISA 240, *The Auditor’s Responsibilities Relating to Fraud in an Audit of Financial Statements* have been expanded or elevated from application material into requirements. We recommend the IAASB consider whether these differences (those related to GAAS are highlighted in appendix B

“Substantive Differences Between the International Standards on Auditing and Generally Accepted Auditing Standards” in the AICPA *Professional Standards* (appendix B)), should be included in the ISAs. We also recommend the IAASB consider enhancing education efforts with users of the financial statements and the auditor’s report to better explain the role of the auditor relating to fraud.

The following is taken from appendix B and contains a listing of requirements that are in GAAS in AU-C section 240, *Consideration of Fraud in a Financial Statement Audit*¹ but are not included as requirements in ISA 240.

- The requirement in paragraph 15 of ISA 240 for the auditor to investigate inconsistent responses to auditor inquiries of management or those charged with governance has been expanded in paragraph .14 of AU-C section 240 to also include responses that are otherwise unsatisfactory (for example, vague or implausible responses).
- The requirement in paragraph 16 of ISA 240 for members of the engagement team to discuss the susceptibility of the entity’s financial statements to material misstatements has been expanded in paragraph .15 of AU-C section 240 to include, as requirements, additional discussion items from application and other explanatory material in ISA 240. These items include a required brainstorming session focused very specifically on, among other things, internal and external fraud factors and the possibility of management override of controls. In addition, AU-C section 240 further clarifies the requirement for participation of key engagement team members and the engagement partner in the discussion and brainstorming sessions. Lastly, AU-C section 240 requires appropriate communication throughout the audit among the engagement team members. Several of these discussion items have been elevated from paragraphs A11–A12 of ISA 240.
- The requirement in paragraph 45 of ISA 240 to document the significant decisions reached during the discussion among the engagement team regarding fraud-related matters has been expanded in paragraph .43 of AU-C section 240 to also require documenting how and when the discussion occurred and the audit team members who participated.
- Procedures have been elevated from paragraph A19 of ISA 240 to requirements in paragraph .19 of AU-C section 240; these procedures relate to making inquiries of internal audit as part of performing risk assessment procedures, and include determining (a) whether internal audit has performed any procedures to identify or detect fraud during the year, and (b) whether management has satisfactorily responded to any findings resulting from these inquiries.
- The requirement in paragraph 35 of ISA 240 to evaluate whether the results of analytical procedures at or near the end of the reporting period indicate a previously unrecognized risk of material misstatement due to fraud has been expanded in paragraph .34 of AU-C section 240 to include the accumulated results of auditing procedures, including analytical procedures performed as substantive tests or when forming an overall

conclusion. AU-C section 240 also specifically requires performance of analytical procedures relating to revenue accounts through the end of the reporting period, in light of the generally presumed higher risk of financial statement fraud involving revenue.

- The requirements in paragraph 33(a) of ISA 240 address designing and performing auditing procedures to test the appropriateness of journal entries. In addition to essential guidance about addressing the risk of possible management override of controls, included in paragraph .32a of AU-C section 240, are requirements to
 - obtain an understanding of the entity's financial reporting process and controls over journal entries and other adjustments, and determine whether such controls are suitably designed and have been implemented.
 - consider fraud risk factors, the nature and complexity of accounts, and entries processed outside the normal course of business, elevated from the application and other explanatory material contained in paragraph A44 of ISA 240 in order to emphasize the importance of these considerations.
 - include identification and testing of specific journal entries regardless of controls.
- The requirement for the auditor to design and perform auditing procedures to review accounting estimates for biases and evaluate whether the circumstances producing the bias, if any, represent a risk of material misstatement due to fraud, in paragraph 33(b) of ISA 240, has been expanded in paragraph .32b of AU-C section 240 to specifically include those estimates that are based on highly sensitive assumptions.

In addition, the following requirements in AU-C section 240 were expanded from the requirements of ISA 240 to be consistent with requirements in PCAOB AS 2410, *Related Parties*,² as the ASB believes these requirements will enhance audit quality for audits of financial statements of nonissuers.

- The requirement in paragraphs 17–19 of ISA 240 relating to required inquiries has been expanded. Paragraph .17 of AU-C section 240 has been expanded to require inquiries of management about the existence, and if so, the nature, terms, and business purpose of, and involvement of related parties in, any significant unusual transactions. Similarly, the requirements in paragraphs .19 and .21 of AU-C section 240 have been expanded to include inquiry about whether the entity entered into any significant unusual transactions.
- The requirement in paragraph 33(c) of ISA 240 for the evaluation of significant transactions that are outside the normal course of business (that is, significant unusual transactions) has been expanded in paragraph .32 of AU-C section 240 to include the following procedures:

² All AS sections can be found in AICPA *PCAOB Standards and Related Rules*.

- Reading the underlying documentation and evaluating whether the terms and other information about the transaction are consistent with explanations from inquiries and other audit evidence about the business purpose (or the lack thereof) of the transaction
- Determining whether the transaction has been authorized and approved in accordance with the entity's established policies and procedures
- Evaluating whether significant unusual transactions that the auditor has identified have been properly accounted for and disclosed in the financial statements

Stakeholder Perspective Question (page 18 of the Discussion Paper): The IAASB is interested in perspectives about requiring the use of forensic specialists or other relevant specialists in a financial statement audit, and, if considered appropriate, in what circumstances the use of specialists should be required.

Response: The ISAs currently contain the following related to the competence and capabilities of the engagement team:

- ISA 220 (Revised), *Quality Management for an Audit of Financial Statements*³ states that “the engagement partner shall determine that members of the engagement team, and any auditor’s external experts and internal auditors who provide direct assistance who are not part of the engagement team, collectively have the appropriate competence and capabilities, including sufficient time to perform the audit engagement.”
- ISA 240⁴ requires the auditor to assign and supervise personnel taking into account the knowledge, skill, and ability of the individuals to be given significant engagement responsibilities and the auditor’s assessment of the risks of material misstatement due to fraud for the engagement.
- Paragraph A35 of ISA 240 provides an example for assigning additional individuals with specialized skill and knowledge, such as forensic and IT experts.

We recommend the IAASB consider expanding the application material in the ISAs or provide nonauthoritative guidance to help auditors identify situations, based on their professional judgment and risk assessment, in which the use of relevant specialists may be needed. For example, this guidance could provide examples of fraud risk factors that may cause the auditor to consider the use of a relevant specialist or could provide examples of circumstances that may cause the auditor to consider using a relevant specialist.

We also encourage the IAASB to explore ways in which engagement teams may be encouraged to better train engagement team members about how frauds occur and what frauds look like, as part of the engagement partner’s fulfilling the responsibilities described above. We also recommend

³ Paragraph 26 of ISA 220, *Quality Management for an Audit of Financial Statements*.

⁴ Paragraph 30 of ISA 240, *The Auditor’s Responsibilities Relating to Fraud in an Audit of Financial Statements*.

the IAASB consider providing more guidance for auditors relating to how to best conduct fraud inquiries and fraud brainstorming, and how auditors may use data analytics or other technologies to enhance their audit procedures around fraud.

IAASB Question 2(b): In your view, is there a need for enhanced procedures [in relation to fraud in an audit of financial statements] only for certain entities or in specific circumstances? If yes:

- (i) For what types of entities or in what circumstances?**
- (ii) What enhancements are needed?**
- (iii) Should these changes be made within the ISAs or outside the scope of an audit (e.g., a different engagement)? Please explain your answer.**

Response: Rather than articulating different requirements for different types of entities, specific procedures to be performed should depend upon the auditor's professional judgment based upon the auditor's risk assessment and the facts and circumstances of the engagement.

As noted in our previous response, we encourage the IAASB to explore ways in which engagement teams can be further trained to better identify fraud risk factors and develop the appropriate audit response in accordance with ISA 315 (Revised 2019) and ISA 330, *The Auditor's Responses to Assessed Risks*, and ISA 450, *Evaluation of Misstatements Identified During the Audit*. Furthermore, as we noted in our cover letter, we encourage the IAASB to continue to develop principles-based standards, without being overly prescriptive considering that these standards may serve as the basis for audits of all entities, whether public or private.

Stakeholder Perspective Question (page 19 of the discussion paper): The IAASB is interested in perspectives about the perceived responsibilities of the auditor regarding non-material fraud in a financial statement audit (i.e., a broader focus on fraud) and what additional procedures, if any, may be appropriate. The IAASB is also interested in perspectives about whether additional audit procedures should be required when a non-material fraud is identified, and if so, what types of procedures.

Response: If the auditor identifies a misstatement, ISA 240 requires the auditor to evaluate whether such a misstatement is indicative of fraud. If there is such an indication, the auditor is required to evaluate the implications of the misstatement in relation to other aspects of the audit, particularly the reliability of management's representations, recognizing that an instance of fraud is unlikely to be an isolated occurrence. Therefore, ISA 240 and ISA 260 (Revised), *Communication With Those Charged With Governance*, already consider non-material fraud. We recommend the IAASB consider the interplay between ISA 240 and ISA 330 as it relates to misstatements of the financial statements relating to fraud. We also note that ISA 240 appears to focus mostly on fraudulent financial reporting, and we encourage the IAASB to consider whether there is a need for further guidance about misappropriation of assets. Such misappropriations may become material when aggregated over several periods.

Stakeholder Perspective Question (page 19 of the Discussion Paper) — The IAASB is interested in perspectives on whether enough emphasis is placed on the auditor's responsibilities around fraud related to third parties. We are also interested in feedback

about the auditor’s role in relation to third party fraud that does not result in a material misstatement of the financial statements but may have a severely negative impact on the entity (e.g., cybercrime attacks).

As noted in the Discussion Paper, the definition of fraud in the auditing standards includes fraud by third parties. We believe that the concept of third-party fraud is not well understood. We recommend the IAASB consider ways to better educate auditors about what is meant by a “third-party” fraud, how such fraud differs from a fraud committed by employees or by those charged with governance, and how such fraud may affect the financial statements.

Stakeholder Perspective Question (page 20 of the discussion paper): The IAASB is interested in perspectives on whether additional engagement quality control review procedures specifically focused on the engagement team’s responsibilities relating to fraud should be considered for audits of financial statements of listed entities, and those other engagements, if any, for which the firm has determined an engagement quality control review is required.

Response: International Standard on Quality Management (ISQM) 2, *Engagement Quality Reviews*, requires the engagement quality control reviewer to discuss with the engagement partner and, if applicable, other members of the engagement team, significant matters and significant judgments made in planning, performing and reporting on the engagement.⁵ The engagement quality control reviewer is also required to review selected engagement documentation relating to the significant judgments made by the engagement team and evaluate: (i) The basis for making those significant judgments, including, when applicable to the type of engagement, the exercise of professional skepticism by the engagement team; (ii) Whether the engagement documentation supports the conclusions reached; and (iii) Whether the conclusions reached are appropriate.⁶

Paragraph 28 of ISA 240 requires the auditor to treat assessed risks of material misstatement due to fraud as significant risks. Accordingly, we recommend the IAASB consider enhancing the application material in ISQM 2 to provide examples of how the engagement quality control reviewer may consider the engagement team’s response to risks of material misstatement due to fraud.

In November 2020, the ASB requested feedback, through a public survey, to the questions in the IAASB Discussion Paper from a U.S. GAAS perspective. Based on the feedback from our outreach initiative, we received examples of factors the engagement quality control reviewer may want to consider, including considering the engagement team’s:

- identification of fraud risk factors and related response,
- brainstorming,
- other procedures performed,
- exercise of professional skepticism, and

⁵ Paragraph 25(b) of ISQM 2, *Engagement Quality Reviews*.

⁶ Paragraph 25(c) of ISQM 2.

- documentation.

IAASB Question 2(c): Would requiring a “suspicious mindset” contribute to enhanced fraud identification when planning and performing the audit? Why or why not?

(i) Should the IAASB enhance the auditor’s considerations around fraud to include a “suspicious mindset”? If yes, for all audits or only in some circumstances?

Response: No. We do not believe requiring a “suspicious mindset” would necessarily contribute to enhanced fraud identification when planning and performing an audit and would potentially have unintended negative consequences on the effective and efficient performance of an audit. For example, a “suspicious mindset” could jeopardize the auditor’s ability to have effective two-way dialogue with management and those charged with governance and ultimately inhibit the auditor’s ability to complete a high-quality financial statement audit. Further, the IAASB standards are defined in the IAASB’s strategy for 2020-2023, as being “globally relevant, forward-looking, applicable to entities of all sizes and complexities, adaptable in an evolving environment, and operable; developed and supported through activities that are independent and free of undue influence, timely, and responsive to the needs of stakeholders.” This approach to setting standards would be free from bias which is counterintuitive to the auditor using a “suspicious mindset.” Accordingly, we believe that professional skepticism is the appropriate mindset for the auditor because the auditor may apply a heightened level of professional skepticism relating to fraud risk, when needed. Further, the concept of professional skepticism is broader than just for fraud and is pervasive throughout the ISAs. We are concerned that requiring a different mindset in certain situations could create confusion in practice as to when it is appropriate for the auditor to use one mindset versus another. We also question whether requiring a suspicious mindset could result in an increased expectation gap.

The ability for the auditor to scale the level of professional skepticism enables the auditor to use his or her professional judgment as to when heightened professional skepticism is necessary. This approach preserves the relationships the auditor needs to effectively audit an entity, including identifying fraud risk factors and developing the appropriate audit response. Accordingly, we are supportive of the existing framework that is used throughout the ISAs of maintaining professional skepticism throughout the audit, having auditors revise their risk assessments when necessary, and having auditors obtain more persuasive audit evidence the higher the assessed risk of material misstatement.

We encourage the IAASB to continue its efforts in regard to the audit evidence project, including consideration of SAS No. 142, *Audit Evidence*, that was issued by the AICPA Auditing Standards Board in July 2020. SAS No. 142 (codified in AU-C section 500) expands the objective of the extant standard to be more broadly focused on considering the attributes of information to be used as audit evidence in assessing whether sufficient appropriate audit evidence has been obtained. Previously, the objective focused on the design and performance of audit procedures to obtain sufficient appropriate audit evidence, rather than evaluating the sufficiency and appropriateness of the audit evidence itself. Attributes of reliable information include its accuracy, completeness, authenticity, and susceptibility to bias. SAS No. 142 requires the auditor to evaluate information

to be used as audit evidence by taking into account the relevance and reliability of the information, including its source, and whether such information corroborates or contradicts assertions in the financial statements. We believe that such enhanced focus on the attributes of reliable information may help auditors to design a more appropriate response to fraud risk.

Stakeholder Perspective Question (page 27 of the discussion paper): The IAASB is interested in perspectives about whether more is needed related to professional skepticism when undertaking procedures with regard to fraud and going concern and what additional procedures, if any, may be appropriate.

Response: As we discussed in our response to IAASB question 2(c), the ability for the auditor to scale the level of professional skepticism enables the auditor to use his or her professional judgment for circumstances when heightened professional skepticism is necessary. This approach enables the auditor to interact with management as needed to effectively audit an entity while planning and performing procedures to identify and assess fraud risks and develop the appropriate audit response.

We note that in recently issued ISAs there has been a heightened focus on professional skepticism in the application material. For example, the application material in ISA 540 (Revised)⁷ describes ways in which the auditor can exercise professional skepticism and ways in which professional skepticism can be documented. We support the IAASB's approach to provide further guidance relating to exercising professional skepticism in the application material for the standards related to fraud and going concern. We recommend that the IAASB consider performing a post implementation review to gather information about how effective the application material in ISA 540 (Revised) relating to professional skepticism has been. We also encourage the IAASB to include application material about professional skepticism specific to fraud and going concern to help improve consistency in the application of the requirements relating to these topics. We believe it would be helpful for the IAASB to provide examples, through nonauthoritative educational materials, that describe ways in which the auditor can exercise and demonstrate heightened professional skepticism in specific circumstances.

IAASB Question 2(d): Do you believe more transparency is needed about the auditor's work in relation to fraud in an audit of financial statements? If yes, what additional information is needed and how should this information be communicated (e.g., in communications with those charged with governance, in the auditor's report, etc.)?

Response: Our response addresses transparency in the auditor's report and transparency through communication with those charged with governance, as follows:

- ***Transparency through the auditor's report.*** We believe that further discussion about fraud in the auditor's report may become fairly boilerplate and would not be meaningful or useful. Rather, we recognize that the IAASB has various options that could be considered to enhance knowledge about the auditor's work in relation to fraud in an audit of financial statements. For example, continued education efforts to help users of the financial statements better understand the role of the auditor as it relates to fraud could

⁷ Paragraph A11 of ISA 540 (Revised), *Auditing Accounting Estimates and Related Disclosures*.

be effective. Further, in light of the IAASB's post implementation review of the auditor reporting standards that began in January 2020, we ask the IAASB to consider the results from this post implementation review before further changes to the auditor's report are proposed.

- ***Transparency through communication with those charged with governance.*** Further communication with those charged with governance about both management's and auditor's responsibilities for fraud and discussing the planned approach and related outcomes of fraud procedures, may be helpful to those charged with governance in executing their financial reporting oversight responsibilities.

Paragraph 28 of ISA 240 requires the auditor to treat those assessed risks of material misstatement due to fraud as significant risks. Therefore, the risks of material misstatement related to fraud are currently required to be communicated with those charged with governance by ISA 260 (Revised). Paragraph 15 of ISA 260 (Revised) states that "the auditor shall communicate with those charged with governance an overview of the planned scope and timing of the audit, which includes communicating about the significant risks identified by the auditor."

Stakeholder Perspective Question (page 29 of the discussion paper): The IAASB is interested in perspectives about whether more information is needed in the auditor's report regarding fraud or going concern, and if so, further details about the transparency needed.

Response: We believe that further discussion about the responsibilities for fraud or going concern in the auditor's report may become boilerplate and would not be meaningful or useful. Further, as noted in our response to IAASB question 2(d), we believe the IAASB should consider the results from the on-going post implementation review relating to the auditor reporting standards before proposing further changes to the auditor's report. Continued education efforts to help users of the financial statements to better understand the role of the auditor as it relates to fraud and going concern would likely be more effective. With regard to fraud, also see our response to IAASB question 2(d). With regard to going concern, also see our response to IAASB question 3(c).

Stakeholder Perspective Question (page 29 of the discussion paper): In addition, the IAASB is interested in perspectives about whether more transparency is needed with regard to communication with those charged with governance.

Response: Further clarification with those charged with governance about their responsibilities, as well as management's and the auditor's responsibilities for fraud may be helpful. We also note that under GAAS, the auditor has an enhanced requirement to communicate to those charged with governance the auditor's consideration of management's plans to mitigate the conditions or events that raised substantial doubt about the entity's ability to continue as a going concern. See our response to the previous stakeholder perspective question.

IAASB Question 3(a): In your view should the auditor have enhanced or more requirements with regard to going concern in an audit of financial statements? If yes, in what areas?

Response: It is the responsibility of management and those charged with governance to first assess the appropriate basis of accounting and whether material uncertainties may cause doubt about the ability of the entity to continue as a going concern. Such responsibilities include determining the appropriate accounting and disclosure in accordance with the applicable financial reporting framework. It is our position that ISA 570 (Revised), *The Auditor's Consideration of an Entity's Ability to Continue as a Going Concern*, adequately addresses the need for management to go "first" and for the auditor to audit management's assessment.

We encourage the IAASB to consider the incremental audit requirements contained in U.S. GAAS related to auditor responsibilities for evaluating going concern in AU-C section 570, *The Auditor's Consideration of an Entity's Ability to Continue as a Going Concern*. We recognize that AU-C section 570 uses different terminology than ISA 570 (Revised) when describing certain concepts and references to accounting terms. The terminology used in GAAS is more commonly used in the United States, for example the use of "substantial doubt." However, the concepts are similar.

The following is a summary of the requirements in GAAS that are not in ISA 570 (Revised):

- AU-C section 570 includes a definition of reasonable period of time that includes the period of time required by the applicable financial reporting framework and also includes application material with examples of the periods contained in various financial reporting frameworks. ISA 570 (Revised) does not include this definition or the related application material.
- AU-C section 570 contains an objective of the auditor to evaluate the possible financial statement effects, including the adequacy of disclosure regarding the entity's ability to continue as a going concern. The ASB believes that the inclusion of this objective is important to address disclosures, particularly for accounting frameworks that contain explicit disclosure requirements. ISA 570 (Revised) does not include this objective.
- AU-C section 570 contains a requirement for the auditor to obtain sufficient appropriate evidence, including written evidence, when management's plans include financial support by third parties or the entity's owner-manager and such support is necessary in supporting management's assertions about the entity's ability to continue as a going concern. This requirement is important to address these situations.
- AU-C section 570 contains a requirement for the auditor to request written representations from management about management's plans to mitigate the adverse effects of conditions or events that indicate there is substantial doubt about the entity's ability to continue as a going concern and the completeness of the financial statement disclosures that management is aware that are relevant to the entity's ability to continue as a going concern. AU-C section 570 also:
 - Includes requirements that address comparative presentations
 - eliminates an emphasis-of-matter paragraph from a reissued report
 - includes a requirement for the auditor to document specific matters related to the auditor's evaluation and conclusions about conditions or events that are identified,

when considered in the aggregate, raise substantial doubt about the entity's ability to continue as a going concern before consideration of management's plans

Further, we encourage the IAASB to consider if and how any proposed changes to the auditor's responsibilities relating to going concern might affect the auditor's responsibilities when auditing financial statements prepared in accordance with a special purpose framework, when auditing a single financial statement, and when engaged to review interim financial information. For example, U.S. GAAS were recently amended to reflect revised auditor responsibilities for assessing going concern and those revisions also included amendments to AU-C section 800, *Special Considerations — Audits of Financial Statements Prepared in Accordance with Special Purpose Frameworks*, AU-C section 805, *Special Considerations — Audits of Single Financial Statements and Specific Elements, Accounts, or Items of a Financial Statement*, and AU-C section 930, *Interim Financial Information*. As circumstances related to going concern would likely be relevant to users of the financial statements in at least some of the situations described in this paragraph, we recommend the IAASB include those sections in their research and consideration of potential changes.

Stakeholder Perspective Question (page 23 of the Discussion Paper) — The IAASB is interested in perspectives on whether entities should be required to assess their ability to continue as a going concern for longer than twelve months, and therefore whether auditors should be required to consider this longer time period in their assessment, beyond the current required period. If stakeholders believe a longer timeframe should be required, alignment will need to be retained between the requirements under the applicable financial reporting framework and the auditing standards in order for auditors to be able to adequately perform their procedures.

Response: We believe that it is important for the financial reporting framework to have an appropriate benchmark for management to consider in determining the appropriate basis of accounting and relevant considerations for addressing uncertainty or doubt regarding the ability of that entity to continue as a going concern, when that basis is applied. From a U.S. perspective, enhancements by the Financial Accounting Standards Board (FASB) to establish a disclosure framework have served to provide helpful transparency about an entity's ability to continue as a going concern and related risks (for example, liquidity, financing and other risks that could adversely affect a company).

We support the concept that the auditor's evaluation of management's assessment of the entity's ability to continue as a going concern should cover the same period as that used by management to make its assessment as required by the applicable financial reporting framework.⁸ However, we also recognize that there may be some financial reporting frameworks that have no explicit requirement. As further explained in our response to IAASB Question 3(a), we encourage the IAASB to consider the incremental audit requirements contained in U.S. GAAS (AU-C section 570) related to auditor responsibilities for evaluating going concern. In particular, AU-C section 570 provides a definition of "reasonable period of time" that includes the period of time required

⁸ Paragraph 13 of ISA 570 (Revised), *The Auditor's Consideration of an Entity's Ability to Continue as a Going Concern*.

by the applicable financial reporting framework, or if no such requirement exists, within one year after the date that the financial statements are issued (or within one year after the date that the financial statements are available to be issued, when applicable). This definition aids the auditor when determining the period of time to be considered.

Stakeholder Perspective Question (page 24 of the discussion paper): The IAASB is interested in perspectives about whether changes are needed with regard to going concern and other concepts of resilience (within the purview of the IAASB’s remit).

Response: We continue to recognize that it is management’s responsibility to assess the entity’s ability to continue as a going concern, as established by the applicable financial reporting framework. Furthermore, we have concerns with introducing new terminology, for example “resilience” because new terminology may cause more confusion and potentially increase the expectation gap. A specific concern is understanding what is meant by “resilience” and how it differs from the concept of “going concern.”

IAASB Question 3(b): In your view, is there a need for enhanced procedures [related to going concern] only for certain entities or in specific circumstances? If yes:

- (i) For what types of entities or in what circumstances?**
- (ii) What enhancements are needed?**
- (iii) Should these changes be made within the ISAs or outside the scope of an audit (e.g., a different engagement)? Please explain your answer.**

Response: We support the concept that audits of all entities should be subject to the same requirements relating to going concern. As we noted in our cover letter, we encourage the IAASB to continue to develop principles-based standards, without being overly prescriptive considering that these standards may serve as the basis for audits of all entities, whether public or private. Also see our response to IAASB question 3(a), as circumstances related to going concern would likely be relevant in at least some circumstances to users of the financial statements prepared in accordance with a special purpose framework, for audits of single financial statements, and when the auditor is engaged to perform an interim review.

IAASB Question 3(c): In your view, do you believe more transparency is needed:

- (i) About the auditor’s work in relation to going concern in an audit of financial statements? If yes, what additional information is needed and how should this information be communicated (e.g., in communications with those charged with governance, in the auditor’s report, etc.)?**

Response: We are concerned that further discussion in the auditor’s report may become boilerplate and would not be meaningful or useful. However, we highlight the following requirements that exist in the applicable financial reporting framework in the United States and correspondingly in the auditing standards for nonissuers in the United States that the IAASB may want to consider as it moves forward with this project:

- Disclosure requirements from the Financial Accounting Standards Board (FASB) include requirements for management to include disclosure in the notes to the financial statements, information when substantial doubt is raised but is alleviated by management's plans. This means, that when substantial doubt about an entity's ability to continue as a going concern is alleviated as a result of consideration of management's plans, the entity is required to disclose information that enables the users of the financial statements to understand (a) the principal conditions or events that raised substantial doubt about the entity's ability to continue as a going concern (before consideration of management's plans), (b) management's evaluation of the significance of those conditions or events in relation to the entity's ability to meet its obligations, and (c) management's plans that alleviated substantial doubt about the entity's ability to continue as a going concern.⁹
- AU-C section 570 includes application material indicating that if the entity has included such a disclosure in the financial statements, and the auditor concludes that substantial doubt has been alleviated by management's plans and adequate disclosure has been made in the financial statements then the auditor may include an emphasis-of-matter paragraph in the auditor's report making reference to management's disclosure.¹⁰

We highlight these U.S. auditing requirements and the corresponding U.S. accounting framework because we believe these requirements in the U.S. jurisdiction provide additional transparency to the users of the financial statements in both the financial statements as well as the auditor's report about events that have raised substantial doubt.

- (ii) **In your view, do you believe more transparency is needed: About going concern, outside of the auditor's work relating to going concern? If yes, what further information should be provided, where should this information be provided, and what action is required to put this into effect?**

Response: One area where more transparency could be helpful to users of the financial statements would be disclosures by management with respect to its evaluation of its ability to continue as a going concern. However, we recognize that this type of transparency is not within the purview of the IAASB.

Additional transparency in the auditor's report with respect to the evaluation of going concern performed by management or other work outside of the auditor's purview may be more confusing than helpful to the users of the financial statements and auditor's report. We encourage the IAASB to undertake appropriate outreach and research before making decisions on this type of additional transparency.

⁹ FASB ASC 205-40-50-12.

¹⁰ Paragraph .A54 of AU-C section 570, *The Auditor's Consideration of an Entity's Ability to Continue as a Going Concern*.



ASB Update: IAASB Project re: Listed Entities and Public Interest Entities

Andrew Prather, ASB Task Force Chair

Presentation at the May ASB 2022 Meeting

Executive Summary



Discussion Objectives

Discuss recent relevant standard-setting developments and planned activities to discern their potential impact to the ASB's 2022-2023 work plan



Standard-Setting Highlights

The PIOB Approved in April 2022 IESBA's revisions to the definitions of "listed entity" and "public interest entity"

PEEC is likely to approve in May 2022 the formation of convergence task force to assess if/how to converge definitions

The IAASB approved in March 2022 its related "two-track" project. The Track 1 ED, focused on auditor independence transparency, is expected to be discussed and approved in June 2022



Big Picture

IESBA has made changes PEEC will need to consider

ASB will need to coordinate with PEEC, while also monitoring IAASB project and providing input

Important for the ASB to provide input to IAASB and consider potential ramifications



Actions

Respond to discussion questions, including the request for additional ASB task force members

Identify if/when ASB standard setting actions are needed

Provide the ASB Task Force recommendations on possible IAASB Track 1 comment letter direction

Recent Standard Setting Developments and Planned Activities

IESBA Update

- In December 2021, IESBA unanimously approved revisions to the definitions of “listed entity” (LE) and “public interest entity” (PIE). Those items were approved by the PIOB in April 2022
- The revised definition of PIEs and new definition of publicly traded entity (see appendix) will become effective for audits of financial statements for periods beginning on or after December 15, 2024 (for audits performed under the International Code of Ethics for Professional Accountants)
- IESBA’s PIE Working Group planned rollout:
 - Chaired by PEEC’s IESBA representative Andrew Mintzer
 - Focused on activities to raise awareness and promote adoption and implementation of the definitions and related provisions in the IESBA Code
 - The IESBA PIE Working Group will be coordinated with the IAASB PIE Task Force



PEEC Convergence Considerations

- The PEEC IFAC Convergence and Monitoring working group is expected to recommend on May 16, 2022 that PEEC form a convergence task force*:
 - Observations:
 - In the U.S., entities covered by the PIE definition are already heavily regulated, and the regulators (e.g., SEC, PCAOB, FDIC, NAIC) require restrictive independence requirements that are generally as restrictive as the IESBA PIE requirements
 - The changes in the IESBA code allow “those bodies responsible for setting ethics standards for professional accountants to more explicitly define” the categories of PIEs (see paragraph 400.18 A1). As a result, PEEC may have some flexibility in how it approaches convergence
 - Anticipated AICPA PEEC Staff Recommendations:
 - The convergence project be given priority so that a refined PEEC definition is available as close as possible to IESBA’s effective date
 - Prefer to avoid having to issue an additional set of independence standards specific to PIEs in the code as well as avoiding the issuance of standards that are inconsistent with those of the applicable regulators



ASB/PEEC Coordination

- Andrew Prather will be the ASB correspondent member on the PEEC convergence task force
- Other opportunities for joint coordination:
 - Joint PEEC/ASB public meetings
 - Off-cycle joint board meetings for executive session
 - Deepened AICPA staff coordination



March 2022 IAASB Highlights

- The IAASB approved in March 2022 a “two-track” project
- The Track 1 ED:
 - Expected to be discussed and approved in June 2022,
 - Is narrowly focused on the mechanism for a firm to disclose whether it has applied the relevant ethical requirements for independence for certain entities, such as PIEs in the IESBA Code
 - By a 12 to 6 vote the IAASB supported exposing a requirement that **when the relevant ethical requirements require transparency** about the specific independence requirements applied, the auditor shall disclose this fact in the auditor’s report
- The Track 2 ED will be focused on:
 - a limited number of targeted changes to the ISQMs and ISAs and
 - developing an objective and guidelines to support the IAASB’s judgments in identifying specific matters for which differential requirements would be appropriate
 - Track 2 has an ED planned for September 2023 and the Final Standard for September 2024

Track 1 ED will also invite/ask respondents to:

1) comment on a potential requirement for the auditor to disclose if specific independence requirements for audits of financial statements of certain entities, as set out in the relevant ethical requirements, were applied

2) Offer alternative disclosure options

Initial ASB Task Force Perspectives Based on the Project Proposal (as of April 2022)

Areas of Agreement

- Convergence objective to reduce term/concept differences
- Streamlining terms/concepts that are substantially the same*

Areas of Concern

- Eliminating ostensibly similar terms could have unintended consequences if not understood how they are currently applied
- Fastrack timeline implies “narrow scope maintenance” but proposed actions may be significant to develop and require additional time (especially when considering other IAASB priorities and resource capacity)
- Intent of proposed differential requirement actions and long-term impacts are unclear
- References to heightened expectations for the independence-related disclosure in the auditor’s report appear to be unsourced

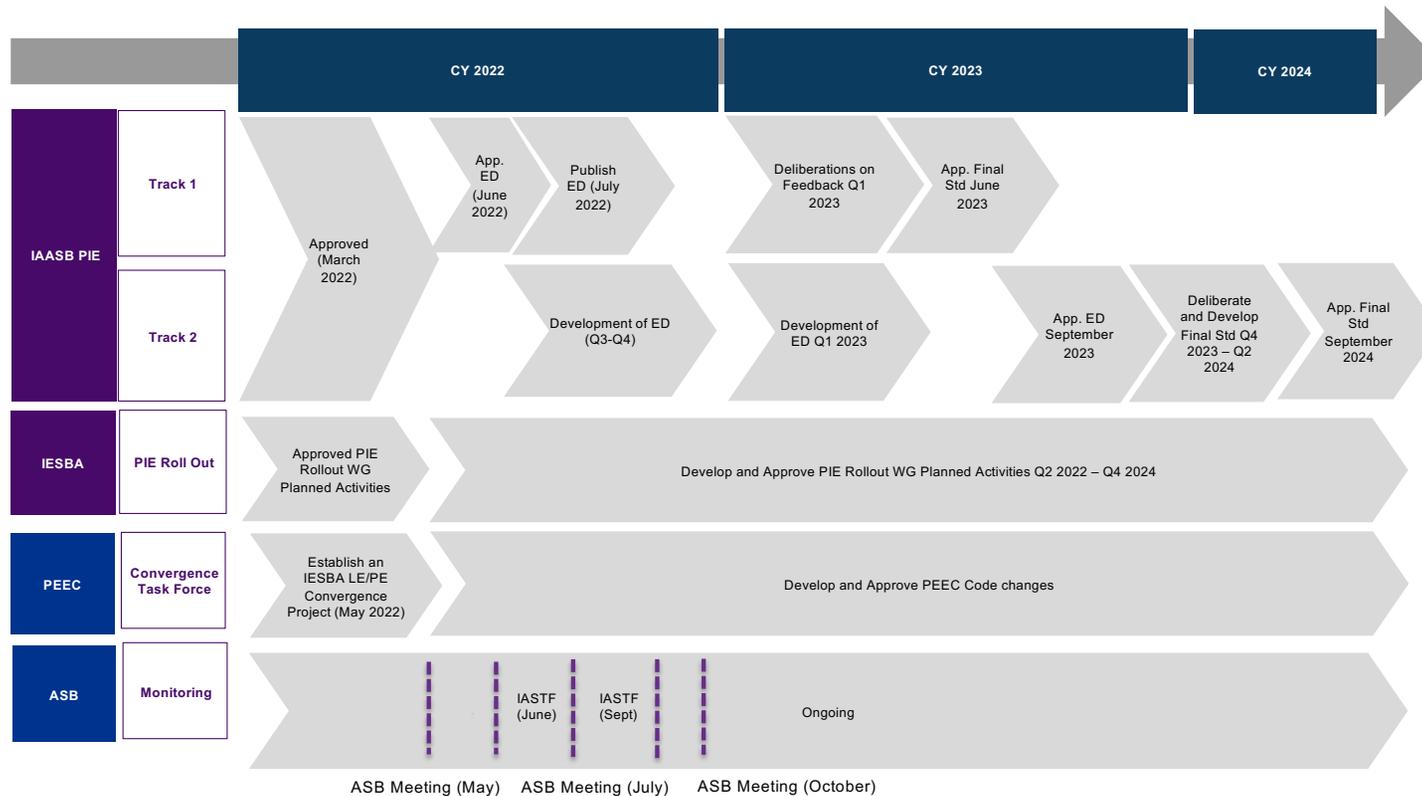
Recommendations

- Need to support the proposal put forth at the March meeting -- a requirement that ***when the relevant ethical requirements require transparency*** about the specific independence requirements applied, the auditor shall disclose this fact in the auditor’s report
- The IAASB should first express and expose a clear rationale and long-term view for establishing differential auditing requirements for PIEs
- Perform “user” outreach, considering recent ISA 700 A30-32 language regarding transparency of independence rules applied and the value for users before determining if the auditor’s report is the best location for disclosing the independence of a firm performing an audit engagement for a PIE

Matters for ASB Consideration

Potential Interdependencies

The following is an overview of relevant standard setting project timelines and potential interdependencies for the ASB to consider:



Questions for the ASB

- Should the ASB consider standard setting changes based on the IAASB's project timeline and thus before PEEC considers what, if any, change will be made to the AICPA code re: listed entities/PIE definitions and transparency requirements?
- What do ASB members believe should be the appropriate frequency and mechanisms for Board-level coordination with PEEC?

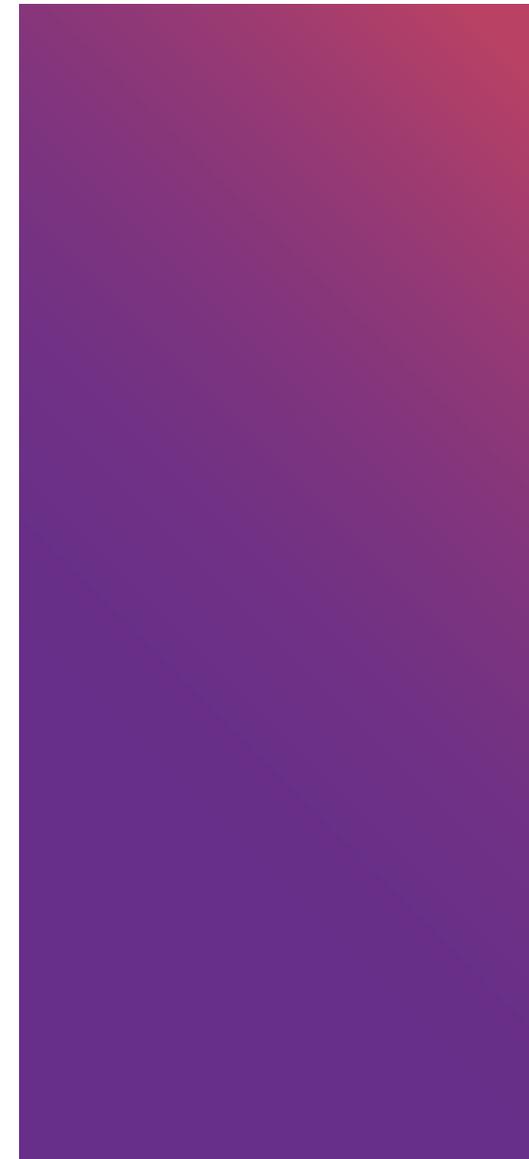
Other Considerations for the ASB

1. Why PEEC and IAASB actions matter:
 - a. If PEEC leaves the PIE definition status quo (i.e., does not amend or significantly change the PIE definition in the Code) then how does the ASB converge with the IAASB, given that the IAASB plans to change its definitions to align with IESBA?
 - b. Potential issue:
 - a. Lack of Code and potential auditing standards convergence between AICPA and IFAC
2. If the ASB wants to take corresponding standard-setting action to follow the IAASB's two track project, can that occur before PEEC complete its actions?
 - a. Are there any issues for the ASB and its convergence objectives?
 - b. Could proactive ASB action cause issues if PEEC has not acted? Maybe not track 1 but track 2?

Appendix

IAASB Project Objectives

Topic	Objective 1: Align Concepts with the Revisions to the IESBA Code	Objective 2: Differential Requirements in ISQMs	Objective 3: Transparency
Key Issues to be Addressed	Increased complexity and inconsistent application when concepts across the IAASB and the IESBA standards differ	Need for more robust and consistent approach to when differential requirements are appropriate	Need for enhanced transparency in the auditor's report about the relevant ethical requirements for independence applied in performing audits for PIEs in the IESBA Code
Project Scope	Adopt the IESBA definition of PIE** and replace "listed entity" with "publicly traded entity"	<p>Develop an objective and guidelines for establishing differential requirements in ISQMs and ISAs</p> <p>Design a case-by-case analysis of extant differential requirements</p> <p>Update application and introductory material in ISQMs and ISAs</p>	Enhance and clarify ISA 700 (revised) to address circumstances when the auditor's report is used to disclose that relevant ethical requirements for independence for certain types of entities
Actions	See Scope above (including related updates to the application material and the glossary)	Establish differential principles, guidelines for establishing differential requirements in the ISAs/ISQMs, and factors used in evaluating the extent of the public interest in the financial condition of the PIE (along with related application and introductory material updates)	<p>Expose a requirement that when the relevant ethical requirements require transparency about the specific independence requirements applied, the auditor shall disclose this fact in the auditor's report</p> <p>Further revise ISA 260 application material to also explain how the auditor would communicate with TCWG</p>
Timing	Track 2		Track 1



Approved Text of the revisions to the IESBA Code as of December 2021:

Public Interest Entities

R400.17 For the purposes of this Part, a firm shall treat an entity as a public interest entity when it falls within any of the following categories:

- (a) A publicly traded entity;
- (b) An entity one of whose main functions is to take deposits from the public;
- (c) An entity one of whose main functions is to provide insurance to the public; or
- (d) An entity specified as such by law, regulation or professional standards to meet the purpose described in paragraph 400.10.

Glossary:

Publicly traded entity:

- An entity that issues financial instruments that are transferrable and traded through a publicly accessible market mechanism, including through listing on a stock exchange.
- A listed entity as defined by relevant securities law or regulation is an example of a publicly traded entity

AICPA Code of Conduct (revised through December 2021):

.41 Public interest entities. All of the following:

- a.* All listed entities, including entities that are outside the United States whose shares, stock, or debt are quoted or listed on a recognized stock exchange or marketed under the regulations of a recognized stock exchange or other equivalent body.
- b.* Any entity for which an audit is required by regulation or legislation to be conducted in compliance with the same *independence* requirements that apply to an audit of listed entities (for example, requirements of the SEC, the PCAOB, or other similar regulators or standard setters).

Additional guidance paragraphs in Approved Text of the revisions to the IESBA Code as of December 2021:

R400.18 In complying with the requirement in paragraph R400.17, a firm shall take into account more explicit definitions established by law, regulation or professional standards for the categories set out in paragraph R400.17 (a) to (c).

400.18 A1 The categories set out in paragraph R400.17 (a) to (c) are broadly defined and no recognition is given to any size or other factors that can be relevant in a specific jurisdiction. The Code therefore provides for those bodies responsible for setting ethics standards for professional accountants to more explicitly define these categories by, for example:

- Making reference to specific public markets for trading securities.
- Making reference to the local law or regulation defining banks or insurance companies.
- Incorporating exemptions for specific types of entities, such as an entity with mutual ownership.
- Setting size criteria for certain types of entities.

400.18 A2 Paragraph R400.17 (d) anticipates that those bodies responsible for setting ethics standards for professional accountants will add categories of public interest entities to meet the purpose described in paragraph 400.10, taking into account factors such as those set out in paragraph 400.9. Depending on the facts and circumstances in a specific jurisdiction, such categories could include: • Pension funds. • Collective investment vehicles. • Private entities with large numbers of stakeholders (other than investors). • Not-for-profit organizations or governmental entities. • Public utilities

Note - Additional guidance appears in paragraphs 400.8, 400.9, 400.10, R400.17, 400.17 A1, 400.19 A1, R400.20, R400.21, R400.22.



ISA 700 – Guidance paragraphs about Independence language in the auditor's report

A 30. In some jurisdictions, relevant ethical requirements may exist in several different sources, such as the ethical code(s) and additional rules and requirements within law and regulation. When the independence and other relevant ethical requirements are contained in a limited number of sources, the auditor may choose to name the relevant source(s) (e.g., the name of the code, rule or regulation applicable in the jurisdiction), or may refer to a term that is commonly understood and that appropriately summarizes those sources (e.g., independence requirements for audits of private entities in Jurisdiction X).

A31. Law or regulation, national auditing standards or the terms of an audit engagement may require the auditor to provide in the auditor's report more specific information about the sources of the relevant ethical requirements, including those pertaining to independence, that applied to the audit of the financial statements.

A32. In determining the appropriate amount of information to include in the auditor's report when there are multiple sources of relevant ethical requirements relating to the audit of the financial statements, an important consideration is balancing transparency against the risk of obscuring other useful information in the auditor's report.

AU-C 700 – Guidance paragraphs about Independence language in the auditor's report

.A38. Relevant Ethical Requirements (Ref: par. .28c). Section 200 explains that ethical requirements consist of the AICPA Code of Professional Conduct together with rules of state boards of accountancy and applicable regulatory agencies that are more restrictive. fn 20 When the AICPA Code of Professional Conduct applies, the auditor's other ethical responsibilities relate to the principles of professional conduct (ET sec. 0.300, "Principles of Professional Conduct").

.A39 Relevant ethical requirements may exist in several different sources, such as ethical codes and additional rules and requirements within law and regulation. When independence and other relevant ethical requirements are contained in a limited number of sources, the auditor may choose to name the relevant sources (for example, the AICPA Code of Professional Conduct, when applicable; the rule or applicable regulation; or Government Auditing Standards promulgated by the Comptroller General of the United States) or may refer to a term that appropriately describes those sources. Relevant ethical requirements, including those pertaining to independence, in a group audit situation may be complex. Section 600, Special Considerations — Audits of Group Financial Statements (Including the Work of Component Auditors), fn 21 provides guidance for auditors in performing work on the financial information of a component for a group audit, including those situations in which the component auditor does not meet the in-dependence requirements that are relevant to the group audit.



Audit Evidence

Discussion of Issues Related to IAASB Project to Revise ISA 500

Kathy Healy, Audit Evidence Task Force Chair

Presentation at the May 2022 ASB Meeting

Executive Summary

Discussion Objectives

- Recap the March 2022 IAASB meeting and current status of relevant issues
- Identify potential ASB monitoring and standard setting actions
- Early identification of recommendations for Wendy Stevens to raise for discussion at the June 2022 IAASB meeting

Key Takeaways

- ASB tentative convergence plan
 - Proposed ISA is generally consistent with SAS 142, but monitoring certain areas
 - Key concepts include clarification of “auditor’s purpose” and proposed revised definition of audit evidence
 - Task Force will consider how best to move forward regarding potential ASB standard-setting action after issuance of ISA

Actions

- ASB members to provide feedback on matters in the slide deck

Relevant Background

- [Status of IAASB Project](#)
 - [IAASB Project Proposal – December 2020](#)
 - The IAASB’s objectives in revising ISA 500 are the same as the objectives that the ASB had in revising AU-C section 500
 - Project is currently in the “exposure draft development” phase
- March 2022 - IAASB discussed proposed revisions to ISA 500 and key issues considered by the IAASB’s Audit Evidence Task Force in drafting the proposed revisions
 - Although broadly supportive, the IAASB asked its task force to further explore and clarify certain areas, which are provided in more detail in slide 6

Relevant Background

- ASB Task Force does not have significant/fatal flaw level concerns with respect to the proposed revisions. However, some issues were communicated to the IAASB that are discussed in subsequent slides
 - TF questioned whether the proposed revisions would result in a change in auditor behavior/action
 - TF concerned about potential differences with SAS 142

March 2022 IAASB Meeting

IASTF Issues Communicated

- Definitions and additional application material
 - While the definitions of *appropriateness (of audit evidence)* and *audit evidence* in proposed ISA 500 (Revised) are streamlined, certain concepts are excluded that will result in challenges to auditor understanding and ultimately to audit quality
- Clarity on documentation requirements
 - Concerned about how the auditor is expected to document his/her *evaluation*
- Information to be used as audit evidence
 - Runs to “auditor’s purpose” issue
- Reliance on technology
 - Proposed ISA provides examples of overreliance on technology – recommend that additional examples be provided to highlight potential under-reliance on technology

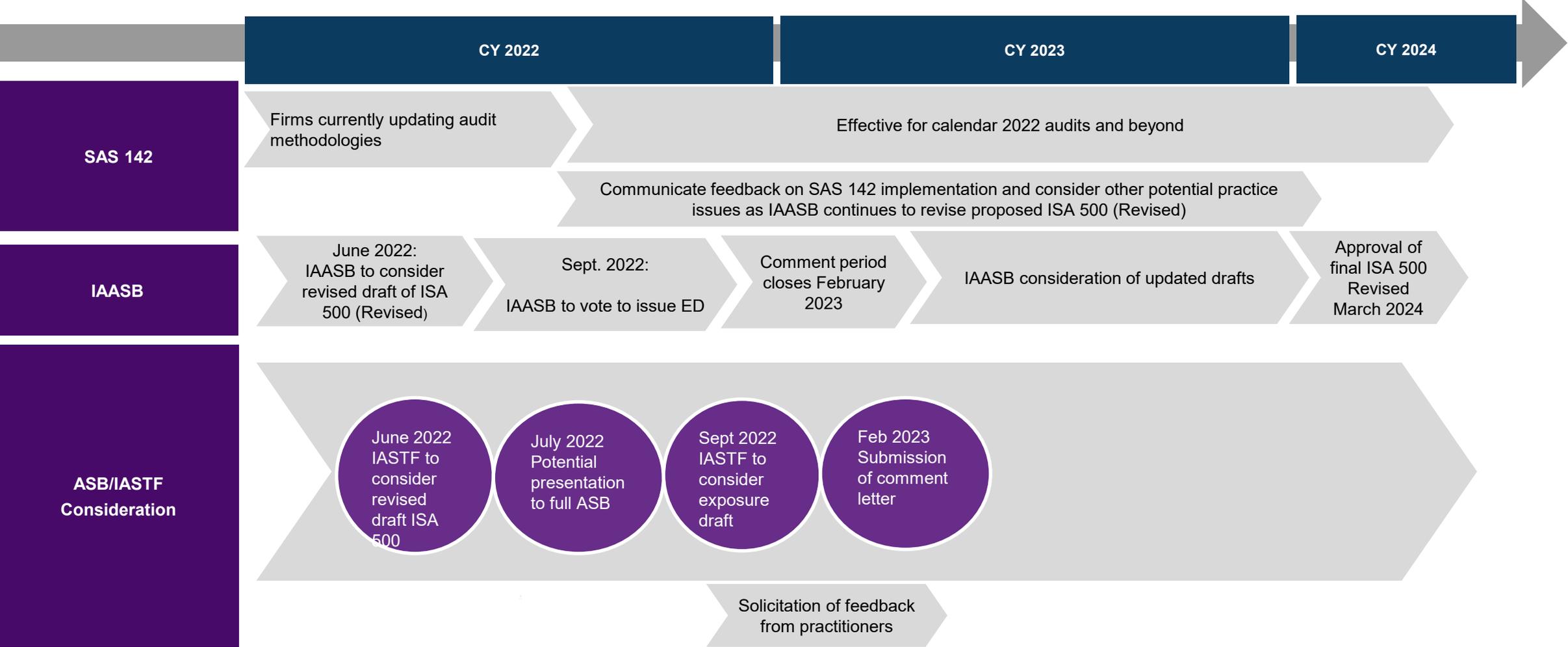
March 2022 IAASB Meeting

IAASB guidance/comments to its task force

- Further explore and clarify the purpose or role of proposed ISA 500 (Revised) in relation to the auditor's responsibility to design and perform audit procedures, including its relationship with the other ISAs
- Confusion on the meaning of the term “auditor’s purposes”
- Further consider the proposed definitions, including whether in all cases information needs to be subject to audit procedures to become audit evidence
- Suggestion to streamline application guidance but enhance certain sections (for example, technology related examples)
- A revised draft of the proposed ISA 500 (Revised) is expected to be presented to the IAASB at its meeting in June 2022

Timeline of *Audit Evidence* Considerations for US Auditors/ASB

The following is an overview of relevant standards and standard setting project timelines related to *audit evidence*



How can ASB inform the IAASB as it develops proposed ISA 500 (Revised)?

- Provide issues identified during implementation of SAS 142
- Feedback on how behavior has been changed (and audit quality enhanced)
 - Different firms, different guidance
- Cost/benefit to implement
 - Level of effort to update methodologies
 - Large firms vs. smaller firm experience

Convergence Issues

- Pursuant to the ASB's Operating Policies, the ASB has a strategic objective to converge its standards with those of the IAASB
- Further, the ASB has a commitment to convergence with the ISAs and to its obligations and responsibilities as an "ISA Base" standard-setter
 - [IFAC's Statements of Membership Obligations](#) formally capture IFAC's longstanding requirement that its member bodies support the work of the IAASB by using their best endeavors to incorporate the ISAs in their national requirements and to assist with the implementation of ISAs

Convergence Issues

- Current draft of proposed ISA 500 (Revised) is generally consistent with SAS 142
 - SAS 142 is effective for calendar 2022 audits
- Post issuance of ISA 500 (Revised), consider the revised ISA along with any post-implementation feedback on SAS 142, as well as
 - Any guidance on changes to AS 1105 from PCAOB
 - Work of ASB's Technology Working Group
- **ASB Members are asked for initial thoughts with respect to any potential revisions to AU-C section 500**

Should the ASB Task Force be doing anything else?

