Australian Government
Auditing and Assurance Standards Board

Agenda

Subject:	**Agenda for the 93rd meeting of the AUASB**
Venue:	**Ken Spencer Room, Auditing and Assurance Standards Board (AUASB) offices Podium Level 14, 530 Collins Street Melbourne**
Time:	**Teleconference: Tuesday, 13 June 2017 from 8.30am to 10.00am.**

Time		Agenda Item No.
8.30am	**1.**	**Welcome**
8.35am	**1A**	**Auditor Reporting**
9.20am	**2.**	**IAASB Agenda item 2** *Quality Control ISQC1*
9.30am	**3.**	**IAASB Agenda item 5** *Quality Control ISA 220*
9.35am	**4.**	**IAASB Agenda item 7** *Group Audits*
9.40am	**5.**	**IAASB Agenda item 4** *Networks*
9.45am	**6.**	**IAASB Agenda item 9** *Professional Scepticism*
9.50am	**7.**	**IAASB Agenda item 3** *Emerging External Reporting (EER)*
9.55am	**8.**	**IAASB Agenda item 8** *Data Analytics*
10.00am	***Close***	

Observers are welcome to participate via teleconference. Please register your interest with Kathleen John at kjohn@aasb.gov.au and on receipt teleconference participant details will be provided.

IAASB International Auditing and Assurance Standards Board
www.iaasb.org

Meeting: IAASB

Meeting Location: New York, USA

Meeting Date: June 19–22, 2017

Agenda Item

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Quality Management (Firm level): Proposed Revisions to ISQC 1[1]

Objective of Agenda Item

1. The objective of this Agenda Item is to obtain the IAASB's input on the Quality Control Task Force's (QCTF) proposals on the revisions to ISQC 1 as a result of incorporating a quality management approach (QMA) into ISQC 1. The input from the IAASB on these matters will assist the QCTF in further developing the revisions to ISQC 1.

QCTF

2. The QCTF comprises the following members:

- Karin French, IAASB Member and Chair of the Task Force
- Bob Dohrer, IAASB Member
- Brendan Murtagh, IAASB Member
- Imran Vanker, IAASB Member
- Josephine Jackson, IAASB Technical Advisor
- Denise Weber, IAASB Technical Advisor
- Keith Wilson, United States Public Company Accounting Oversight Board (official observer)
- Dawn McGeachy, IFAC Small and Medium Practices Committee Representative (correspondent member)

Activities of the QCTF

3. Since the March 2017 IAASB meeting, the QCTF has had one physical meeting and two teleconferences.

4. In developing the proposals in this Agenda Item, the QCTF formed a sub-group, comprising two task force members and Staff (referred to as the drafting team). The drafting team has had one physical meeting since its formation in January 2017 and several teleconferences. Given the success of the drafting team in furthering the development of ISQC 1, the QCTF plans on continuing to use this as a mechanism for drafting the revisions to ISQC 1 going forward.

5. Since the March 2017 IAASB meeting, the Chair of the QCTF and Staff held a teleconference with a representative of the International Ethics Standards Board for Accountants (IESBA) to discuss the outcome of the IAASB's March 2017 discussion with respect to the eligibility of the engagement quality control reviewer and to consider further actions that could be taken in this regard.

[1] International Standard on Quality Control (ISQC) 1, *Quality Control for Firms that Perform Audits and Reviews of Financial Statements, and Other Assurance Engagements and Related Services Engagements*

Matters for IAASB Consideration

6. **Agenda Item 2–A** sets out the discussions and views of the QCTF in developing the revisions to ISQC 1, and includes the matters for IAASB consideration. The IAASB is asked to consider the matters set out in this Agenda Item.

7. **Agenda Item 2–B** includes a working draft of ISQC 1. The purpose of this document is to demonstrate the proposals of the QCTF and how they would be reflected in ISQC 1. However, the proposed requirements and application material in this Agenda Item require further refinement once the IAASB has provided its views on the proposals on this topic.

8. **Agenda Item 2–C** includes the QCTF's proposed prescribed quality objectives, quality risks and responses that would be ultimately incorporated into ISQC 1. These are illustrative only and the QCTF will further consider these requirements, including whether additional or more enhanced requirements are necessary in response to respondents' views to the IAASB's Invitation to Comment (ITC), *Enhancing Audit Quality in the Public Interest: A Focus on Professional Skepticism, Quality Control and Group Audits*. The QCTF is not, at this stage, seeking the IAASB's views on specific aspects of the proposed requirements in this Agenda Item.

9. **Agenda Item 2–D** contains a mapping of the requirements in extant ISQC 1 to the proposed requirements in **Agenda Item 2–B** and **Agenda Item 2–C.**

10. The **Supplement to Agenda Item 2** includes a summary of the responses to the ITC, as well as the names of the respondents to the ITC.

Material Presented

Agenda Item 2–A	*Quality Management (Firm level): Proposed Revisions to ISQC 1*
Agenda Item 2–B	*Quality Management (Firm level) Working Draft of ISQC 1*
Agenda Item 2–C	*Quality Management (Firm level) Prescribed Quality Objectives, Quality Risks and Responses*
Agenda Item 2–D	*Quality Management (Firm level) Tracking Document of Requirements in Extant ISQC 1 to new Proposals*
Supplement to Agenda Item 2	*Summary of Responses to the ITC*

IAASB Discussion

11. Each of the QCTF members will participate in presenting this topic to the IAASB at the June 2017 meeting. An outline of the topics for discussion, the QCTF member presenting the topic and the approximate timing of the discussion is included below.

Topic	QCTF Member Presenting
Introduction	Karin French
Components of ISQC 1 and Terminology	Karin French
Robustness and Scalability	Karin French
Governance and Leadership, including Organization, Culture and Strategy	Brendan Murtagh
Information and Communication	Bob Dohrer

Topic	QCTF Member Presenting
Quality Management Process	Josephine Jackson and Denise Weber
Monitoring and Remediation	Imran Vanker
Interconnectedness of the Components	Karin French
Changing Behaviors	Karin French
Next Steps	Karin French
Separate Standard Addressing EQC Reviews	Karin French

Appendix A

Minutes from the March 2016 IAASB Meeting

Quality Control – ISQC 1

Eligibility of the Engagement Quality Control (EQC) Reviewer

Ms. French provided an overview of the Quality Control Task Force's (QCTF) proposals in relation to the eligibility of the EQC reviewer, which included the QCTF's recommendations to address the time that an individual who had previously been involved in the audit would not be eligible to fill the role of the EQC reviewer (the cooling-off period). Ms. French also highlighted the feedback from the CAG Representatives at their recent March 2017 meeting, as well as the views of the Small and Medium Sized Practices (SMP) Committee.

CRITERIA FOR SELECTION OF AN EQC REVIEWER

The Board was supportive of the overall direction proposed by the QCTF and encouraged a principles-based approach. The Board provided the following additional suggestions:

- The Board noted that there could be circumstances when the EQC review is performed by a group of reviewers and encouraged the QCTF to acknowledge such circumstances.
- The Board was of the view that the EQC reviewer's authority is created through the processes established by the firm's system of quality management. The Board indicated that the proposals regarding the relationship between the firm's culture and the EQC reviewer's authority were confusing and therefore encouraged clarity regarding how the firm's culture influences the EQC reviewer's authority. The Board also noted that the chain of command in relation to the EQC reviewer could impact the EQC reviewer's authority and objectivity and recommended that this be specifically discussed in the standard.
- The Board encouraged the QCTF to provide clarity on the distinction between technical competence and practical experience and emphasized the importance of attaining an appropriate balance between the attributes. The Board also noted that in some jurisdictions the EQC reviewer is required to be licensed which could further limit the number of individuals that are eligible to perform the EQC review. The Board also recommended that the criteria for the eligibility of the EQC reviewer should be linked to the basis for which the engagement is subject to an EQC review, however did not consider that it is always necessary for the EQC reviewer to have experience in relation to listed entities.
- The Board recommended that the provisions regarding the degree to which the EQC reviewer may be consulted should be retained, as these had been diluted in the proposed revisions.
- The Board encouraged the QCTF to further consider how the proposals would relate to engagements that are non-audit engagements.

OBJECTIVITY OF THE EQC REVIEWER

The Board agreed that further coordination with the IESBA should be undertaken, taking into consideration the respective remits of the two Boards. The Board did not support the IAASB undertaking revisions to the IAASB Standards in the absence of the IESBA taking further steps to address the issue. The Board provided the following additional comments in relation to the objectivity of the EQC reviewer:

- Certain members raised concern that the proposed requirements in relation to the objectivity of the EQC reviewer appear more onerous than the provisions in relation to an engagement partner.
- The Board noted that not all jurisdictions apply the IESBA Code and therefore cautioned against proposals that would be specific to the IESBA Code.
- The Board was of the view that a further understanding is needed regarding the basis for IESBA's cooling-off period of three years in relation to an EQC reviewer. The Board encouraged the QCTF to consider a two year cooling-off period (similar to the period prescribed by the Public Companies Accounting Oversight Board) and to further understand the effect of the proposed cooling-off period on SMPs.

THE PROCESS FOR THE SELECTION OF THE EQC REVIEWER

The Board was supportive of the QCTF's proposals in relation to the firm's selection of the EQC reviewer, however suggested that the exemption, "unless, in exceptional circumstances, it is not practicable", be reconsidered as it is unlikely to be an exceptional circumstance in the case of SMPs.

IAASB CAG Chairman's Remarks

Ms. Lang highlighted that the CAG Representatives emphasized the importance of achieving an appropriate balance with respect to the criteria for the eligibility of the EQC reviewer and questioned how the proposals would be implemented and enforced. Furthermore, Ms. Lang noted that many IAASB CAG Representatives are also IESBA CAG Representatives, and accordingly were supportive of the cooperation with the IESBA on this topic.

PIOB Observer Remarks

The PIOB encouraged the IAASB to further coordinate with the IESBA with respect to the cooling-off period.

Quality Management (Firm level): Proposed Revisions to ISQC 1[1]

The minutes from the IAASB's discussion on quality management in December 2016 are included in the Appendix of this Agenda Item. **Agenda Item 2** includes the minutes of the IAASB's March 2017 discussion in relation to engagement quality control reviews that form part of ISQC 1.

Objective of the IAASB Discussion

The objective of this Agenda Item is to obtain the IAASB's input on the Quality Control Task Force's (QCTF) proposals on the revisions to ISQC 1. In particular, the QCTF seeks the IAASB's views on the following matters:

- How the quality management approach (QMA) has been incorporated into ISQC 1.
- The overall structure of ISQC 1, including how the components interrelate, and how they would be implemented in practice.
- The scalability of the revisions to ISQC 1 and its application by small and medium sized practices (SMPs).
- The robustness of the proposed revised ISQC 1.
- The proposed direction in relation to the requirements addressing:
  - Governance and leadership, including organization, culture and strategy.
  - Information and communication.
  - The quality management process (QMP), including monitoring and remediation.
- The appropriate location of the requirements and application material in relation to engagement quality control (EQC) reviews.
- How the proposals would change firm behaviors.

The input from the IAASB on these matters will assist the QCTF in further developing the revisions to ISQC 1.

Introduction

1. In 2013, the IAASB published its findings on its post-implementation review of the clarified International Standards on Auditing (ISAs) that highlighted the need for further consideration about aspects of quality control. Issues in relation to firm's systems of quality control have been consistently highlighted in inspection findings by audit regulatory bodies and audit oversight bodies, and in dialogue with these stakeholders. In addition to these issues, the IAASB recognizes the increasing needs of SMPs, including the adaptability of ISQC 1 to the nature and size of the firm.

2. In December 2015 the IAASB published the Invitation to Comment (ITC), *Enhancing Audit Quality: A Focus on Professional Skepticism, Quality Control and Group Audits,* in order to explain the issues in relation to ISQC 1 and to obtain stakeholder's feedback on possible actions the IAASB could take to address the issues. Many respondents to the ITC agreed that the public

[1] International Standard on Quality Control (ISQC) 1, *Quality Control for Firms that Perform Audits and Reviews of Financial Statements, and Other Assurance Engagements and Related Services Engagements*

interest issues highlighted in the ITC were relevant and agreed that further actions should be pursued to address them.

3. As a result, in December 2016 the IAASB approved a project proposal for the revision of ISQC 1 to strengthen and improve a firm's management of quality for all engagements performed under the IAASB's International Standards by enhancing the requirements and application material and more explicitly incorporating a QMA.

4. At the December 2016 IAASB meeting, the QCTF introduced their initial recommendations on integrating a QMA within ISQC 1. This included recommendations on how the structure of ISQC 1 would be revised and how the scalability[2] principles of a QMA could be encapsulated in the standard, while maintaining the robustness of ISQC 1. Furthermore, in March 2017 the QCTF presented these proposals to the CAG. The appendix includes the minutes of the IAASB's December 2016 meeting and extracts of the draft minutes of the CAG's March 2017 meeting relevant to this paper. This Agenda Item discusses the QCTF's further recommendations on the proposed revisions to ISQC 1 and includes recommendations in response to the IAASB and CAG's feedback.

5. **Agenda Item 2–B**, **Agenda Item 2–C** and **Agenda Item 2–D** accompany this issues paper. **Agenda Item 2–B** includes a working draft of ISQC 1 and **Agenda Item 2–C** includes the QCTF's proposed prescribed quality objectives, quality risks and responses (i.e., the application of the QMA). The purpose of these accompanying agenda items is to demonstrate to the IAASB how the proposals of the QCTF would be executed. However the proposed requirements and application material require further refinement and development once the IAASB has provided its views on the matters set out in this Agenda Item. **Agenda Item 2–D** contains a mapping of the requirements in extant ISQC 1 to the proposed requirements in **Agenda Item 2–B** and **Agenda Item 2–C**.

6. This paper sets out the QCTF's proposals in relation to:

   (a) Governance and leadership, including organization, culture and strategy;

   (b) Information and communication (excluding documentation); and

   (c) The QMP, including monitoring and remediation.

   These proposals are based on the feedback from the IAASB and the CAG, as well as the comments from respondents to the ITC (the Supplement to **Agenda Item 2** includes an analysis of the comments from respondents on these topics).

7. This Agenda Item also explores the options in relation to the location of the requirements and application material with respect to EQC reviews.

8. As noted above, this paper includes a discussion on "information and communication" that forms part of the component "information, communication and documentation". This paper does not include a discussion on "documentation" since the QCTF is of the view that this can only be properly considered once all of the other components of ISQC 1 have been further developed.

9. The QCTF continues to deliberate the other discrete topics that form part of a firm's system of quality management, including EQC reviews, transparency reporting, engagement partner performance and rewards, and engagement partner competency and human resources. The

[2] The QCTF recognizes that there are different interpretations of the meaning of the terminology "scalability" and "proportionality." For the purposes of this paper, the term "scalability" has been used to represent both scalability and proportionality, and therefore scalability means (i) whether or not the requirement applies to the firm based on its circumstances; and (ii) if the requirement applies, the extent to which the requirement can be applied in a manner commensurate with the size and complexity of the firm.

QCTF is of the view that these topics could affect the following aspects of the proposals set out in the accompanying agenda items:

(a) The prescribed quality objectives, quality risks and responses in **Agenda Item 2–C** are likely to be affected by the QCTF's proposals in relation to EQC reviews, engagement partner performance and rewards, and engagement partner competency and human resources. Furthermore, although the prescribed quality objectives, quality risks and responses in **Agenda Item 2–C** are based on the requirements in extant ISQC 1, the QCTF has yet to fully consider these requirements, for example, whether additional or more enhanced requirements are necessary or how to further introduce scalability into these requirements.

(b) The information and communication component in **Agenda Item 2–B** may be affected by the QCTF's proposals with respect to transparency reporting.

The QCTF plans to further consider these topics after the June 2016 IAASB meeting and will present its recommendations to the IAASB in September 2017.

Components of ISQC 1 and Terminology

10. In December 2016 and March 2017, the QCTF presented the proposed components of the firm's quality management to the IAASB and the CAG respectively. Both were generally supportive of the proposed components and provided various additional suggestions. Nevertheless, the QCTF noted the IAASB's confusion regarding the use of terminology in describing the quality management system, for example, the difference between "quality management" and the "quality management process", as well as what is considered to be components of quality management and elements of applying the QMP. While the QCTF recognizes that certain components of quality management are not strictly part of a "system", the use of the term "system of quality management" is easier to comprehend and is similar to the current terminology in ISQC 1 (i.e., "system of quality control"). Furthermore, this term would assist in differentiating the entire system of quality management from the "QMP". Accordingly, the QCTF proposes that throughout ISQC 1, the term "system of quality management" should be used.

11. The QCTF deliberated the use of the terms "foundational component", "component" and "element" that were used to describe the various parts of the firm's system of quality management. The QCTF noted that while these terms would have limited use in ISQC 1, it is important to use them consistently to avoid unnecessary confusion. Accordingly, the QCTF determined that the following terms would have the related meaning:

(a) Component refers to the three interactive concepts within the system of quality management (as illustrated in the diagram in paragraph 16):

- Governance and leadership, including organization, culture and strategy.
- Information, communication and documentation.
- QMP

The requirement in paragraph 21 of **Agenda Item 2–B** requires the firm to establish and maintain a system of quality management that includes these components.

(b) Element refers to the elements of the firm's system of quality management that exist in extant ISQC 1, however exclude leadership responsibilities for quality within the firm and

monitoring as these form part of the components described above.[3] It is noted that the elements have not been retained in their current state in the proposed revisions to ISQC 1, as further explained in paragraph 82.

(c) QMA refers to the concept of a risk-based approach to managing quality that forms the basis for the revisions to ISQC 1.

(d) QMP refers to the component within the firm's system of quality management that establishes requirements for firms in relation to quality objectives, quality risks and responses, and includes monitoring and remediation.

12. The QCTF also considered the various other suggestions from the IAASB related to the use of terminology, for example, replacing the term "responses" with "controls". The QCTF continues to believe that the terminology used by the QCTF in its initial drafting remains appropriate in order to minimize confusion with other frameworks that use similar terms with different meanings, for example, the use of the word "controls" in the COSO Internal Control – Integrated Framework.[4]

13. The QCTF considered whether the component of "organization, culture and strategy that foster quality" should be a stand-alone component, as recommended by the IAASB. As explained in paragraphs 26–33, the QCTF is of the view that the firm has a responsibility to establish governance principles in relation to quality and implement such principles through various actions, including through assigning responsibility and accountability for quality to firm leadership. In this context, the QCTF debated how "organization, culture and strategy that foster quality" would exist as a stand-alone component since these concepts are encompassed within the governance principles and the responsibilities of firm leadership. Accordingly, the QCTF recommends that the component of "governance and leadership" should instead be titled "governance and leadership, including organization, culture and strategy", as these are all linked and inseparable. Furthermore, by including "organization, culture and strategy" together with leadership, the QCTF is of the view that leadership's responsibility for these factors is further emphasized.

14. The QCTF also considered the following:

(a) Whether "documentation" is a subset of information and communication, i.e., whether it should be incorporated in the title of the component. The QCTF is of the view that documentation has many purposes, which may be additional to the function of information and communication, for example, documentation is a mechanism to evidence the firm's compliance with ISQC 1. Accordingly, the QCTF recommends that "documentation" remain in the title of this component.

(b) The prominence of the component "monitoring and remediation" in the context of the firm's system of quality management. The QCTF remains of the view that this forms part of the QMP, and has sufficient prominence in ISQC 1 (paragraphs 38–50 of **Agenda Item 2–B**).

(c) Whether "re-evaluating the QMP" should be a discrete component. The QCTF agreed that the firm should re-evaluate their QMP, however this would be part of the iterative, ongoing cycle within the QMP, rather than a periodic step. This iterative, ongoing evaluation is established through the proposed requirements and application material in the working draft. In particular:

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[3] These elements comprise (i) relevant ethical requirements, (ii) acceptance and continuance of client relationships and specific engagements, (iii) human resources, and (iv) engagement performance.

[4] Committee of Sponsoring Organizations of the Treadway Commission (COSO), Internal Control – Integrated Framework

- In establishing quality objectives and identifying and assessing quality risks (including considering the continued relevance of the quality objectives and quality risks), the firm needs to be responsive to changes in the factors and circumstances affecting the firm (e.g., a new service offering, changes in the firm's environment) or other information (e.g. the results of monitoring activities) (paragraphs A52, A57 and A70 of **Agenda Item 2–B**).
- As part of the monitoring activities, the firm is required to design monitoring activities that include an evaluation of the QMP, including the appropriateness of the quality objectives and whether the QMP is appropriately identifying, assessing, and responding to the quality risks (paragraph 39(c) of **Agenda Item 2–B**).
- As part of the remediation process, when deficiencies are identified, the firm's evaluation of the effects of the deficiencies include a consideration of the continued relevance of the firm's quality objectives, including whether all quality risks have been identified and appropriately assessed and whether the responses to quality risks remain appropriate (paragraph 46(b) of **Agenda Item 2–B**).

15. It was suggested by the CAG that the term "applying the QMP" was misleading since "applying a process" is illogical and may not be sufficiently clear that this component includes requirements. Paragraphs 58–86 of this Agenda Item further explore the QCTF's recommendations in relation to the prescribed quality objectives, quality risks and responses that have been developed based on the elements of a system of internal control set out in extant ISQC 1 and how these would be integrated into ISQC 1.

16. Based on the recommendations of the QCTF set out above, the proposed structure of ISQC 1 would be as follows:

(a) Governance and leadership, including organization, culture and strategy.

(b) Information, communication and documentation.

(c) QMP:

(i) Establish quality objectives;

(ii) Perform quality risk assessment;

(iii) Design and implement responses to quality risks; and

(iv) Monitor and remediate.

Matter for IAASB Consideration

1. Does the IAASB agree with revising the terminology to refer to the "firm's system of quality management" instead of "the firm's quality management"?

[Note: Further questions on the specific components and the proposed changes have been included in the respective sections of this Agenda Item addressing such components.]

Robustness and Scalability

17. **Agenda Item 2–B** demonstrates how the proposals of the QCTF would be executed, and **Agenda Item 2–D** contains a mapping of the requirements in extant ISQC 1 to the proposed requirements in **Agenda Item 2–B** and **Agenda Item 2–C**. The QCTF is of the view that the robustness of ISQC 1 has been retained and enhanced through:

    (a) Establishing governance principles in relation to quality that firms are required to implement through various actions, thereby providing a consistent guideline for firms in creating an environment that sustains and improves quality, and enhancing the requirements addressing the responsibilities of firm leadership.

    (b) Improving the requirements related to information and communication, to give more recognition to the continual, iterative process of obtaining or generating and communicating information in order to support the functioning of the firm's system of quality management, and emphasize the importance of both internal and external communication.

    (c) Introducing the "QMP" that compels the firm to think about the relevant quality objectives and quality risks, based on its circumstances and environment, and identify responses that are targeted to addressing such risks. By identifying and managing quality risks, the firm is focused on areas of quality risk and opportunities for improvements may be identified. Furthermore, the QCTF is of the view that such a process encourages the firm to respond on a periodic and ongoing basis to changes in the firm's circumstances or other information relevant to the firm's system of quality management.

    (d) Improving the requirements related to monitoring and remediation, and introducing the concept of a causal analysis that compels the firm to understand the underlying cause(s) of deficiencies, thereby improving how the firm responds to those deficiencies through remedial actions. The proposals also require the firm to take into consideration information from external inspections in establishing the scope and frequency of its monitoring activities and in identifying and remediating deficiencies.

    (e) Retaining the requirements that exist in the elements of extant ISQC 1 through establishing them as prescribed quality objectives, quality risks and responses that are applicable to all firms.[5]

18. In accordance with the proposals in the ITC, the QCTF is continuing to explore the other topics that may require further enhancement in ISQC 1 that may also improve the robustness of the standard, including EQC reviews, networks, transparency reporting, engagement partner performance and rewards, and engagement partner competency and human resources.

19. While the robustness of ISQC 1 has been improved, the QCTF is cognizant of feedback from respondents that the standard needs to be scalable to the size, nature and structure of the firm. Accordingly, when developing the proposed requirements in ISQC 1, the QCTF considered different strategies for specifically conveying the intended scalability of the standard. In particular, the QCTF considered the following:

    (a) Are the requirements essential to a firm's system of quality management, i.e., "think small first"?

    (b) Are the requirements applicable to all firms in all circumstances, for example, perhaps the requirement should be conditional for certain circumstances?

[5] **Agenda Item 2–C** includes the QCTF's proposed prescribed quality objectives, quality risks and responses, as well as a mapping of these proposals to the extant requirements in ISQC 1.

(c) How could the requirements be articulated to demonstrate their scalable application, for example, could application material explain the flexibility of the application?

For example, with respect to the requirement for the firm to establish governance principles in relation to quality and implement them through various actions, the QCTF noted that audit firm governance codes have been established in some jurisdictions, which contain detailed requirements for firm's governance, and corporate governance codes also typically contain many specific requirements. The QCTF determined that granular requirements would be too onerous for many firms and not relevant in all circumstances, and accordingly developed the four essential principles (paragraph 22 of **Agenda Item 2–B**), which the QCTF believes to be relevant in all cases. These principles are also outcome-based to further promote scalability, i.e., it is up to the firm to determine how these principles are actually achieved. The proposed application material acknowledges that jurisdictional codes may exist or firms may identify more extensive governance principles, in order to encourage firms to determine whether additional governance principles are relevant. However, for SMPs the four essential principles may be adequate.

20. The basis of the QMP is that the firm determines quality objectives and quality risks, based on its circumstances and environment and identifies responses that are targeted to address such risks. Nevertheless, as a safeguard to support the consistent and robust application of the QMP by firms, the standard includes prescribed quality objectives and quality risks that exist across all firms, and for which there are required responses (**Agenda Item 2–C**). Undertaking the QMP will necessitate effort by the firm in identifying quality objectives, quality risks and responses relevant to the firm that are supplementary to those set out in the standard, particularly in the first year of implementation. However, the outcome of this, if properly undertaken by the firm, will result in an improved system of quality management that focuses the firm's resources on areas of risk, and may eliminate any redundant activities currently performed by the firm. Although the firm will have a responsibility to reconsider the quality objectives, quality risks and responses as a result of changes and other information, the frequency of such considerations will depend on a variety of factors, for example, the rate of change of the firm's circumstances and deficiencies identified (i.e., if the system of quality management is effective and there are no changes in the firm's circumstances, the need to reconsider the quality objectives, quality risks and responses would be less likely).

21. There are other areas in the QCTF's proposals that introduce and highlight the flexibility and scalability of the standard. In addition to those described above, some examples include:

(a) The outcome-based nature of the requirements related to information and communication.

(b) Allowing the firm to choose the nature of the response to quality risks, i.e., whether the firm chooses policies, procedures, processes or other methods as a response.

(c) Empowering the firm to determine the scope and frequency of the monitoring activities, which are driven by a variety of factors.

(d) Requiring the firm to consider the nature, timing and extent of the causal analysis procedures based on the nature of the deficiencies.

(e) Highlighting in application material how the quality objectives and quality risks may be established within the firm, i.e., that larger and more complex firms may establish quality objectives at a firm level, and cascade more granular quality objectives to various levels within the firm, while smaller and less complex firms may cascade more granular quality objectives directly to the engagement level.

Furthermore, the introductory section and related application material explains the importance of scalability, for example, by referring to the system of quality management being tailored to the circumstances of the firm.

22. In considering mechanisms to enhance the scalability of ISQC 1, the QCTF debated whether to retain the sections in the application material "Considerations Specific to Smaller Firms". The QCTF noted that for a proper understanding of how the firm's system of quality management should be set up and tailored to the circumstances of the firm, it is necessary to explain examples and considerations in relation to SMPs in the application material in the context of the matter, rather than discrete pieces that may be out of context or misunderstood if read in isolation. Furthermore, the QCTF is of the view that this guidance may be equally applicable to other firms, given that the system of quality management is inherently scalable. Accordingly, with a few exceptions, the sections in relation to "Considerations Specific to Smaller Firms" have been integrated into the application material as examples.

23. The QCTF recognizes that several new requirements have been introduced, and other requirements have been enhanced. The QCTF is of the view that the volume of the application material may need to increase in order to provide the necessary information to assist firms in understanding the new requirements and enable consistent application in practice (the QCTF notes the support from respondents to the ITC for additional application material across many topics). These revisions, together with extensive application material that has been proposed by the QCTF, may appear overwhelming. In this regard, the QCTF will continue to explore how to position the application material, in order to facilitate a reduced volume, for example, through the use of appendices or possibly a Staff Publication to assist with initial implementation. The QCTF also plans to continue consideration of how the ISQC 1 can be enhanced to address scalability as it further progresses the draft of the standard.

Matters for IAASB Consideration

2. Is the IAASB of the view that the proposals would result in the robustness of ISQC 1 being retained, and in some cases enhanced?

3. The IAASB is asked to share their views regarding the QCTF's proposals to improve and emphasize the scalability of ISQC 1. In particular:

   (a) Does the IAASB have any further recommendations on how scalability could be introduced in the standard, while retaining the necessary robustness?

   (b) Does the IAASB agree with the QCTF's recommendation to include examples and considerations in relation to SMPs in the application material in the context of the matter, rather than retaining the sections "Considerations Specific to Smaller Firms"?

Governance and Leadership, including Organization, Culture and Strategy

24. The ITC noted that ISQC 1 does not address firm governance, nor contain much detail as to what is expected from firm leadership in relation to firm governance, and therefore included various suggestions to address firm governance and enhance the role of firm leadership in sustaining and continually improving audit quality. These suggestions included:

   (a) Seeking opportunities to enhance ISQC 1 to emphasize the importance of governance and a focus on quality at all levels within a firm, including through the use of a QMA.

   (b) Clarifying leadership responsibilities to more explicitly incorporate commonly used and familiar terminology (e.g., "tone at the top" and "leading by example").

(c) Emphasizing the importance of firm leadership setting an appropriate culture for the firm and for taking responsibility and being accountable for extending that culture throughout the firm.

(d) Considering whether there should be a requirement for accountability of firm leadership, or appropriate personnel within firm leadership, for matters related to quality.

(e) More specifically requiring a firm to identify appropriate personnel within the firm's leadership to be responsible and accountable for independence matters.

(f) Explicitly incorporating the concept of the public interest into ISQC 1 and emphasizing the importance of relevant public interest considerations in relation to the design of the firm's system of quality control.

The QCTF recognized the overall support from respondents for the proposed actions, although any actions would need to be flexible to accommodate different jurisdictions and firm structures.

25. The QCTF presented an overview of the proposals in relation to governance and leadership to the CAG at their March 2017 meeting. The CAG Representatives were supportive of the proposed direction, and emphasized the importance of firm leadership assuming ultimate responsibility and accountability for quality. The CAG further encouraged the QCTF to consider the practicality of introducing governance principles in the circumstances of SMPs. Accordingly, in developing the requirements, the QCTF considered the applicability of the governance principles to SMPs and how the requirements could be tailored to the circumstances of a broad range of firms. A further discussion of the QCTF's approach is included in paragraph 19.

Governance

26. A firm's governance is of paramount importance to quality since it is the way in which the firm embeds its culture and ethics and self-regulates, and serves as the framework for how the firm's decisions are made. A firm's governance also affects the public's perception of the firm; a firm without effective governance may be regarded as one that does not operate in the public interest. Accordingly, the QCTF is of the view that establishing governance principles would provide a consistent guideline for firms in establishing an environment that sustains improves engagement quality.

27. The QCTF recognizes that firms operate in a variety of environments and have different structures. Accordingly, the QCTF proposes introducing a requirement for the firm to establish governance principles in relation to quality and implement them through various actions. The proposed requirement also requires the firm to include certain governance principles set out in ISQC 1 (i.e., principles that the QCTF proposes to be applicable to all firms in all circumstances). Such an approach allows firms the flexibility to identify the most suitable governance principles, since in some circumstances more specific governance principles may be appropriate while in other circumstances the essential principles set out in ISQC 1 may be adequate. The proposed principles have been articulated in an outcome-based manner, which provides firms with flexibility in determining how the principles will be achieved.

28. In developing the principles, the QCTF considered numerous sources, including the following:

- *A Framework for Audit Quality: Key Elements that Create an Environment for Audit Quality* (Audit Quality Framework).
- The United Kingdom *Audit Firm Governance Code*, revised in July 2016.
- The draft *Principles for Effective Management of Audit Firms (The Audit Firm Governance Code)* recently issued in Japan.

- The *Irish Audit Firm Governance Code*, issued in January 2013.
- The United Kingdom's Financial Reporting Council publication *Corporate Culture and the Role of Boards Report of Observations*.
- The Royal Netherlands Institute of Chartered Accountants publication *Measures to Improve the Quality and Independence of the Audit in the Netherlands*.
- The COSO *Enterprise Risk Management Framework* (June 2016 edition exposed for public commentary).
- The Organization for Economic Co-operation and Development (OECD) *G20/OECD Principles of Corporate Governance*.
- The *King IV Report on Corporate Governance for South Africa (2016)*.

29. The QCTF noted that any governance principles would need to be internationally applicable and relevant to the overall objective of ISQC 1, i.e., supporting quality. Many of the sources highlighted above address governance from a commercial perspective, and the QCTF is of the view that given the scope of ISQC 1, it would be inappropriate to extend the governance principles beyond those necessary to support quality. Furthermore, while some of these sources include principles or requirements that may be highly effective in addressing quality, certain of these principles or requirements are not practically applicable to all types of firms, or would be difficult to mandate at an international level, for example, the creation of a separate governing board. Accordingly, although the governance principles recommended by the QCTF are based on these sources, they are not established at a similar level of specificity.

30. The four overarching governance principles that have been identified by the QCTF are as follows (paragraph 22 of **Agenda Item 2–B**):

    (a) *The firm's internal culture fosters quality, including professional and ethical values, to support the firm's public interest role:*

    The firm's internal culture is an important factor in influencing how the firm's personnel function in the interests of the public, while at the same time working towards the accomplishment of the firm's commercial goals. Paragraph 18 of extant ISQC 1 requires the firm to establish policies and procedures to promote an internal culture that recognizes the importance of quality. However, it does not explain the importance of quality in supporting the firm's public interest role. In addition, the fundamental responsibility of firm leadership in embedding such a culture is not evident. Accordingly, along with the introduction of the governance principle set out above, the QCTF has proposed creating a more explicit link to firm leadership's responsibilities in relation to culture (paragraph 23(a) of **Agenda Item 2–B**).

    In addition to these improvements, the QCTF has proposed the addition of detailed application material, in response to feedback on the ITC, that:

    - Explains why culture is so important to the firm's system of quality management (paragraph A12 of **Agenda Item 2–B**).
    - Emphasizes the role of all personnel in the firm in relation to the firm's culture (paragraph A13 of **Agenda Item 2–B**).
    - Provides examples of actions that can be undertaken by firm leadership to embed the culture (paragraph A13 of **Agenda Item 2–B**).

(b) *The firm is organized in a manner that supports the effective design, implementation and operation of the firm's system of quality management:*

The organization of the firm encompasses:

- Establishing an internal firm structure;
- Designating authority and responsibility within the firm; and
- Maintaining and allocating sufficient and appropriate resources.

Establishing a structure within the firm and determining who in the firm is responsible for aspects of quality is critical to enabling decision-making and supporting the functioning of the system of quality management. The QCTF recognizes that certain jurisdictions prescribe the structure of the firm or the composition of the firm leadership and in many cases this has resulted in recognized improvements in firm governance. However, it is not practicable for ISQC 1 to do so, given its international application and the varying circumstances across firms and jurisdictions. Nevertheless, the QCTF is of the view that establishing the organization of the firm as a governance principle would have the effect of compelling firms to consider how to organize the firm in a manner that supports the effective design, implementation and operation of the firm's system of quality management.

(c) *The firm has effective leadership with responsibility and accountability for quality.*

Under extant ISQC 1, firm leadership is assigned ultimate responsibility for the firm's system of quality control. Paragraph 35 to 38 below explain the QCTF's recommendations in relation to improving the requirements regarding the responsibility and accountability of firm leadership. These requirements descend from the governance principles, i.e., the governance principles establish the overall framework for the environment that is necessary to support quality, while the requirements regarding the roles and responsibilities of firm leadership support the implementation of those principles.

(d) *The firm enhances stakeholder confidence in the public interest aspects of the firm's decision-making in relation to quality.*

The firm may have a variety of stakeholders, including the network or other network firms, audit oversight bodies and other external bodies, those charged with governance of the firm's clients or users of the firm's reports. Stakeholders' perception of the quality of engagements performed by the firm is improved when they consider that the firm supports and embeds a quality-focused culture that emphasizes the firm's public interest role. Accordingly, the QCTF is of the view that a fundamental guiding principle is that the firm should be cognizant of its stakeholder needs and take actions to build their confidence in the firm's decision-making. Furthermore, it encourages the communication with the firm's stakeholders about its commitment to quality.

31. The governance principles form the basis for the firm's decisions and how it acts in terms of the effects on quality, and therefore closely relate to the other components of ISQC 1. For example, in establishing the quality objectives, the firm considers whether the objectives are aligned with the firm's governance principles, or as part of its communication strategy, the firm considers the needs of its external stakeholders.

32. The QCTF debated how the requirement for these governance principles should be established, for example, whether the requirement should indicate that the firm shall apply these principles. The QCTF concluded that the requirement should focus on the firm establishing governance principles in relation to quality, thereby allowing the firm to consider additional principles that may be relevant in their circumstances.

33. In addition to establishing the governance principles, the QCTF noted that the firm would need to implement them through various actions in order that the outcome of the principles are achieved. Such actions would include those set out in the various proposed requirements of ISQC 1, including (i) assigning ultimate responsibility and accountability for quality to firm leadership and requiring firm leadership to take actions that address each of the principles, (ii) the firm's monitoring and remediation activities, and (iii) the responses the firm puts in place to address quality risks. In addition to these requirements, the firm may implement the governance principles through other actions that are further explained in the application material relating to governance and leadership.

34. An action that is of particular importance, and is a key element in many of the governance frameworks researched, relates to establishing a whistleblowing mechanism. Extant ISQC 1 includes this requirement, commonly known as "complaints and allegations", in the monitoring section of the standard. The QCTF debated whether it would remain appropriate for these requirements to form part of monitoring, or whether they are more suited to supporting the firm's application of the governance principles. The QCTF agreed that it would be best placed within governance given its importance to establishing the culture of the firm and to avoid the perception that complaints and allegations are only addressed through the firm's monitoring processes (paragraphs 26–27 of **Agenda Item 2–B**).

Leadership

35. As highlighted above, one of the governance principles includes having effective leadership with responsibility and accountability for quality, since firm leadership has a critical role in sustaining and continually improving quality. Firm leadership also has a responsibility to take actions to implement all of the governance principles established by the firm, for example, leadership is the key driver of the internal culture that fosters quality and establishes the professional and ethical values that support the firm's public interest role.

36. Under paragraph 18 of extant ISQC 1, the firm's chief executive officer (or equivalent), or the firm's managing board of partners (or equivalent) are required to assume ultimate responsibility for the firm's system of quality control. However, the QCTF is of the view that this requirement needs to be enhanced to further emphasize the importance of quality and to reflect firm leadership's responsibilities with respect to the governance principles. Accordingly, the QCTF proposes the following enhancements to the requirements addressing the responsibility of firm leadership (paragraph 23 of **Agenda Item 2–B**):

    (a) Extending the responsibility beyond the firm's system of quality control to being responsible for quality. Under extant ISQC 1, the focus is on firm leadership's responsibility for the firm's system of quality control. However, in the view of the QCTF, firm leadership's responsibility is broader and should focus on the ultimate objective of ISQC 1, i.e., quality.

    (b) Introducing accountability for quality. Under extant ISQC 1, the focus is on the responsibility of firm leadership, while accountability is not mentioned. As these are different concepts, albeit interrelated, the QCTF is of the view that firm leadership should also be accountable for quality. Respondents to the ITC had also supported the suggestion to introduce accountability for quality in relation to firm leadership. This new requirement in relation to accountability for quality is supported by proposed application material that explains how accountability may be established and links accountability for quality to evaluating the effectiveness of firm leadership overall, as well as the performance of individuals within firm leadership (paragraph A28 of **Agenda Item 2–B**).

(c) Explicitly highlighting the responsibility of firm leadership to conduct themselves in a manner that promotes the firm's culture and extends the culture throughout the firm. This aligns with the governance principle relating to the firm's culture and is consistent with the proposals in the ITC regarding firm leadership's responsibility for culture. While firm leadership needs to act in a way that embeds the culture, there are other actions that firm leadership can take to further extend the culture throughout the firm. The proposed application material explores some examples of how this can be undertaken (paragraph A13 of **Agenda Item 2–B**).

(d) Highlighting that firm leadership establishes a business strategy that is reflective of the firm's values and the importance of quality. The firm's business strategy defines how it will operate and accordingly is key to integrating quality within the firm. The QCTF noted the guidance in the Audit Quality Framework emphasizing the delicate balance between profitability and the need for the firm to achieve quality in all engagements, as well as paragraph A5(b) of extant ISQC 1 that discusses the assignment of management responsibilities so that commercial considerations do not override the quality of work performed. One member of the QCTF was of the view that commercial considerations have a fundamental impact on quality and therefore a requirement should specifically acknowledge the fact that commercial considerations should not override quality. However, other members of the QCTF were of the view that this could remain in application material, since commercial considerations are unlike the other leadership responsibilities as they are not associated with an action of leadership and therefore would be inconsistent. Furthermore, these members noted that balancing quality and commercial considerations would be an output of applying the governance principles and implementing the leadership actions.

(e) Highlighting firm leadership's role in establishing sufficient and appropriate resources. Providing the appropriate resources to support the firm's system of quality management is essential to its proper functioning, and firm leadership is in a position of power to influence the extent of the firm's resources and how they are allocated.

(f) Highlighting firm leadership's responsibilities in relation to the other governance principles, i.e., the organizational structure and stakeholder confidence.

37. The QCTF agreed that it needs to be clear who is responsible and accountable for the firm's system of quality management, and considered the references in extant ISQC 1 to the firm's chief executive officer (or equivalent) or, if appropriate, the firm's managing board of partners (or equivalent). The QCTF agreed that the current references are still relevant, but is of the view that further clarification is needed. In particular, in circumstances when the firm does appoint a managing board of partners, it would be inappropriate for the firm to allocate the responsibility and accountability for quality to a sole individual as may be currently implied in ISQC1. This is because other individuals on the managing board of partners are also in a position to influence the quality, culture and resources of the firm and may inappropriately do so if they are not equally responsible or accountable. Accordingly, the phrase "if appropriate" has been removed in referring to the firm's chief executive officer (or equivalent) or the firm's managing board of partners (or equivalent) and application material has been introduced to explain that in circumstances when there is a managing board of partners, that the entire managing board is responsible and accountable for quality and resources (paragraph A19 of **Agenda Item 2–B**).

38. In order to further embed the accountability of firm leadership, the QCTF is of the view that the performance of firm leadership needs to be evaluated (paragraph 25 of **Agenda Item 2–B**). The QCTF noted the performance evaluation of firm leadership is in fact a monitoring activity and debated whether it would be appropriate for this evaluation to extend to those person(s) that are

assigned operational responsibility for the firm's system of quality management. The QCTF concluded that given the importance of the role of such individual(s), it is important for them to also be evaluated. The QCTF agreed that it would be important to take appropriate action in response to the outcome of such performance evaluations and a requirement has been included to this effect. Application material that highlights who may perform the evaluation has also been included (paragraph A28 of **Agenda Item 2–B**). The QCTF will further explore application material to support aspects of such evaluations, in conjunction with the QCTF's work on engagement partner performance and rewards that will be presented to the IAASB in September 2017.

Resources

39. Under extant ISQC 1, the provisions in relation to resources focus on human resources, however there are many other types of resources that are necessary to support the firm's system of quality management and the performance of engagements, including financial resources, human resources, technology resources and intellectual resources (e.g., the firm's methodology or guides). Such resources do not only relate to resources directly utilized by engagement teams. Firms may require resources that indirectly support the performance of engagements, for example, a technical team and the resources needed to support the functioning of the technical team.

40. As a result, the QCTF is of the view that firm leadership's responsibilities related to resources discussed above should include all resources. Furthermore, the broader meaning of resources (i.e., including financial resources, human resources, technology resources and intellectual resources) is used in the QMP in relation to the prescribed quality risks and responses that are related to resources (**Agenda Item 2–C**).

Responsibility for the Firm's System of Quality Management

41. The QCTF has proposed retaining the requirement in paragraph 19 of extant ISQC 1 that addresses the experience, ability and authority of individuals who are assigned operational responsibility for the firm's system of quality management, although this has been enhanced with the addition of "accountability" of such individuals. Furthermore, the QCTF proposes the addition of application material that includes examples of how the firm may organize itself in terms of assigning operational responsibility for the system of quality management and how accountability may be established.

Responsibility for Independence Matters

42. The QCTF noted the mixed views from respondents to the ITC regarding the proposals for a requirement for the firm to identify appropriate personnel within firm leadership to be responsible and accountable for independence matters.

43. The QCTF is of the view that firm leadership is ultimately responsible and accountable for independence matters. Nevertheless, firm leadership may assign operational responsibility for compliance with the independence requirements within the firm, for example, in the case of a large firm the operational responsibility may be assigned to a particular partner. In such circumstances, the QCTF agreed that the individual(s) should have sufficient and appropriate experience and authority in the firm to assume that responsibility, and that a requirement in this regard would be appropriate.

44. The QCTF further agreed that assigning responsibility for the independence process would be a firm's response to the risk of non-compliance with the firm's independence requirements. Accordingly, the requirement would be placed in the QMP section (refer to R4 in **Agenda Item**

2–C). The QCTF noted that this approach would be consistent with how assigning responsibility for the monitoring process has been addressed in paragraph 42(a) of **Agenda Item 2–B**.

Other Matters

45. The ITC proposed incorporating the concept of "public interest" into ISQC 1 and emphasizing the importance of relevant public interest considerations in relation to the design of the firm's system of quality management. The QCTF noted respondent's overall mixed views about explicitly referring to the public interest. Nevertheless, the QCTF is of the view that firms should be reminded of their role with respect to the public interest, and actions the firm can take to enhance their consideration of their public interest role. Accordingly, throughout the requirements and application material in this component, the QCTF has proposed several references to the firm's public interest role where relevant.

46. The QCTF noted the extensive support from respondents to the ITC for firm leadership to be more involved in monitoring the effectiveness and appropriateness of updated policies and procedures and remedial actions. As indicated in paragraph 44, the QCTF is of the view that specific responsibilities should be included in the sections to which they relate, and accordingly this has been incorporated in monitoring and remediation (paragraph 48 of **Agenda Item 2–B**).

47. In order to demonstrate the interconnectedness of the various components and to reinforce that information and communication is essential to each component of the firm's system of quality management, emphasis has been given to effective communication in the application material in the governance and leadership section (e.g., embedding the firm's culture and communicating roles and responsibilities within the firm).

Matters for IAASB Consideration

4. Paragraph 13 discusses the QCTF's recommendation to combine "organization, culture and strategy that foster quality" with governance and leadership into a single component. Does the IAASB agree with this recommendation, particularly in light of the proposed requirements and application material in relation to this section?

5. Does the IAASB agree with the QCTF's recommendation to introduce a requirement for firms to establish governance principles in relation to quality and to implement them through various actions? If so:

   (a) Is the IAASB of the view that the four governance principles identified by the QCTF are appropriate?

   (b) Are there additional governance principles that should be included?

6. The IAASB is asked to share their views regarding the QCTF's proposals in relation to firm leadership, in particular the following:

   (a) Does the IAASB agree that the responsibilities of firm leadership should be extended beyond being responsible for the system of quality control as is currently required by ISQC 1, i.e., that firm leadership should be responsible for quality?

   (b) Does the IAASB agree that in circumstances when the firm has appointed a managing board of partners, that the full managing board of partners is responsible and accountable for quality, as proposed in paragraph 37?

   (c) Does the IAASB agree that there should be an assignment of operational responsibility for compliance with the independence requirements, and that such person(s) should

possess sufficient and appropriate experience and authority in the firm to assume that responsibility?

(d) Does the IAASB agree with the introduction of a requirement for the firm to establish periodic performance evaluations that assess the effectiveness of the person(s) that are assigned ultimate responsibility or accountability for quality and does the IAASB support this being extended to any person(s) that are assigned operational responsibility for the firm's system of quality management?

(e) Does the IAASB agree with the specific responsibilities identified in paragraph 23(a)–23(e) of **Agenda Item 2–B** and are there additional responsibilities that have not been identified that should be considered?

(f) Does the IAASB agree with the conclusion of the QCTF that the requirements related to "complaints and allegations" are necessary in supporting the firm's culture and accordingly should be incorporated in the component "Governance and Leadership, including Organization, Culture and Strategy"?

7. Does the IAASB support the proposal to include references to public interest throughout the requirements in relation to "Governance and Leadership, including Organization, Culture and Strategy", in order to remind firms of their role with respect to the public interest and actions the firm can take to enhance their consideration of their public interest role?

Information and Communication

48. At the December 2016 meeting, the discussion in relation to quality control included the importance of information, communication and documentation to the firm's system of quality management. Communication includes having appropriate communication resources (e.g., information systems infrastructure) to communicate information about quality across the firm and to provide timely and relevant information to the firm's leadership regarding the operation of the firm's system of quality management. The IAASB supported the QCTF's proposal that a number of revisions could be made to ISQC 1 related to the firm's information systems and communication processes.

49. The QCTF also presented its initial proposals with respect to information and communication to the CAG in March 2017 and noted the overall support from the CAG on the proposed improvements, in particular for increased emphasis on communication with external parties. The CAG also noted the importance of transparency reporting. The QCTF is continuing to discuss the topic of transparency reporting, and plans to present its recommendations to the IAASB in September 2017.

50. In exploring possible revisions to ISQC 1 to address information and communication, the QCTF considered other frameworks and sources that address information and communication, in particular the COSO Integrated Framework and the COSO Enterprise Risk Management Framework.[6] The QCTF noted that both COSO frameworks also acknowledge the importance of information and communication as essential components of a system of quality management.

51. As indicated in the COSO Integrated Framework, communication is the continual, iterative process of providing, sharing and obtaining necessary information. The QCTF observed that under extant ISQC 1 the focus is on the firm's communication down to personnel, and gives little acknowledgement of the iterative nature of communication and the fact that information may come from a variety of sources. Accordingly, the proposed requirements in relation to information

[6] The COSO Enterprise Risk Management Framework, released for public exposure in June 2016.

and communication include the following to emphasize the range of parties with whom communication may need to take place, and to highlight the two-way nature of communication:

(a) A discussion of the various parties internal and external to the firm with whom communication may take place that demonstrates how information may be disseminated (paragraph 28(a)–28(c) of **Agenda Item 2–B**). This is further explained in paragraph 52.

(b) A specific requirement for the firm to establish policies or procedures that facilitate the communication of information relevant to the firm's system of quality management with the relevant parties. The two-way nature of communication is further emphasized through highlighting that such information enables *the firm and the relevant parties* to take appropriate and timely action (paragraph 28 of **Agenda item 2–B**).

52. The QCTF identified the various information sources and stakeholders with whom two-way communication may take place, for incorporation in the requirement described above. These include:

(a) Engagement teams who may need information in order to perform their engagements and may need to provide information to the firm that is necessary for the functioning of the firm's system of quality management.

(b) Personnel performing functions in relation to the operation of the firm's system of quality management who may need information to understand their roles and responsibilities and perform these functions. Likewise, these personnel may need to feed information up to the firm.

(c) Firm leadership who needs information in order to fulfill their oversight responsibilities for the firm's system of quality management. Similarly, firm leadership has a key role in communicating information down into the firm, for example, in embedding the firm's culture.

(d) Parties external to the firm who may need a variety of information. Such parties may include the network, network firms, external oversight authorities, users of the firm's reports or the firm's clients, external service organizations, or the firm's legal counsel. Similarly, the firm may need information from these parties.

53. In addition to the requirement that specifies the various stakeholders, the QCTF has proposed application material that explains:

(a) The type of information that may be communicated between these stakeholders (paragraphs A38–A41 of **Agenda Item 2–B**).

(b) The attributes of information that need to exist in order for the firm to place reliance on the information (paragraph A36 of **Agenda Item 2–B**). These attributes are similar to those related to information quality in the COSO Integrated Framework.

(c) The effectiveness of communication is dependent on the consistency of the matters communicated, the timeliness of the communication and the methods adopted by the firm to communicate the information (paragraph A44 of **Agenda Item 2–B**). This application material may encourage the firm to consider how to communicate information effectively.

54. The QCTF recognized that the other components of the firm's system of quality management may need to contain specific requirements regarding communication. For example, there are communication requirements in relation to monitoring and remediation and the firm is required to establish processes to address whistleblowing. The QCTF agreed that it would be appropriate for such requirements to remain in the components to which they relate, instead of incorporating them within the information and communication section, given that information and communication is pervasive to all of the components of the system of quality management (i.e.,

specific requirements in the overall section of communication and information may undermine the universal nature of information and communication).

55. Nevertheless, the QCTF is of the view that linking the information and communication section to the specific requirements in the components is valuable in emphasizing how information and communication applies in relation to the components. For example, paragraph A13 of **Agenda Item 2–B** (relating to "governance and leadership, including organization, culture and strategy") references to the firm's responsibilities related to information and communication. Similarly paragraph A52 of **Agenda Item 2–B** (relating to "establish quality objectives") highlights that the firm may consider the continued relevance of the quality objectives or whether all relevant quality objectives have been identified as a result of information, such as the results of monitoring activities or information communicated by engagement teams related to the firm's system of quality management.

56. Information and communication are also prevalent in the quality risks and responses that form part of the QMP. The QCTF noted that in some cases the risks would arise because of insufficient information and therefore certain quality risks and responses identified in **Agenda Item 2–C** also include matters specifically related to information and communication.

57. In addition, the firm's monitoring activities include an evaluation of the firm's information and communication and whether it enables and supports the proper functioning of the firm's system of quality management, which is a proposed requirement in paragraph 39(b) of **Agenda Item 2–B**. A cross-reference to this requirement has been included in the application material in the information and communication component.

Matters for IAASB Consideration

8. The IAASB is asked to share their views regarding the proposed requirements and application material addressing information and communication, in particular:

   (a) Does the IAASB believe that these appropriately emphasize the importance of two-way communication?

   (b) Do the proposed requirements and application material highlight the pervasive nature of information and communication, including that it is a continual, iterative process of providing, sharing and obtaining necessary information?

   (c) Does the IAASB agree that specific requirements related to communication should be located in the sections of ISQC 1 to which they relate?

Quality Management Process

58. At the December 2016 meeting, the IAASB noted that the QMP would be an area that would be particularly challenging for SMPs to implement and provided various suggestions on the concepts proposed by the QCTF. The QCTF remains of the view that the firm should establish quality objectives, identify and assess quality risks and design and implement responses to the quality risks, and the QCTF's thinking on how this would be established in ISQC 1 is further explained below. In developing the requirements related to the QMP, the QCTF considered other frameworks and sources that contain similar concepts, in particular the COSO Integrated Framework and how the ISAs have addressed a risk-based approach.

59. In December 2016, the QCTF also proposed an additional component of the firm's system of quality management, "applying the QMP." The QCTF envisioned that this would contain the elements in extant ISQC 1, converted to quality objectives, quality risks and responses consistent with the principles of a QMA. These quality objectives, quality risks and responses derived from

the elements in extant ISQC 1 would be relevant to all firms in all circumstances (these are referred to as "the prescribed quality objectives, quality risks and responses" in this Agenda Item). Since then, the QCTF debated how the proposed new requirements to establish quality objectives, identify quality risks and responses to such risks would be practically applied to the elements and the QCTF has developed its initial proposals in this regard.

Establish Quality Objectives

60. The overall objective of ISQC1 is set out in paragraph 16 of **Agenda Item 2–B** and the various requirements across all of the components contribute to achieving that objective. The QCTF debated whether it is necessary for the firm to establish quality objectives specific to the firm's circumstances that support the overall objective of ISQC 1, and form the basis for the identification and assessment of quality risks.[7] As part of this debate, the QCTF also considered how the quality objectives to be established by the firm would relate to the prescribed quality objectives.

61. The QCTF concluded that in supporting the notion that the firm's system of quality management is tailored to the circumstances of the firm, the quality objectives would need to be relevant to the circumstances of the firm and set at an appropriate level of granularity. Furthermore, the quality objectives should facilitate the identification and assessment of quality risks, and accordingly would need to be sufficiently granular to support this. The QCTF agreed that consistency in the granularity of the quality objectives across firms would not be necessary, as some firms may identify high-level objectives that are equally as effective in providing a basis for the identification and assessment of quality risks as firms that cascade more granular quality objectives to various levels within the firm.

62. While ISQC 1 would establish prescribed quality objectives, these would not be established at a level of granularity, given the broad range of circumstances across firms and the fact that the quality objectives support the overall objective of ISQC 1. Accordingly, the expectation would be that the firm would use the prescribed quality objectives in ISQC 1 as a basis for the establishment of more relevant and granular quality objectives.

63. However, the QCTF agreed that the prescribed quality risks and responses would need to be set at a more granular level in order to capture the elements in extant ISQC 1 and to address the additional enhancements to ISQC 1 that were suggested in the ITC. The QCTF noted that the requirement for the firm to establish quality objectives would have a different approach from the requirements in relation to the firm's identification of risks and design of responses. This would be the case because the quality objectives established by the firm would be derived from the prescribed quality objectives. Conversely, the quality risks identified by the firm would be more granular than the prescribed quality risks or additional to the prescribed quality risks, i.e., the prescribed quality risks would not identify all possible quality risks as these would need to be specific to the firm's circumstances. The same principle would apply to the responses.

64. The QCTF has therefore proposed a requirement for the firm to establish quality objectives and for the firm to consider the relevance and granularity of the quality objectives (paragraphs 30–31 of **Agenda Item 2–B**). This is supported by application material to explain that the relevance and granularity of the quality objectives may change, for example, as a result of new information or changes in factors and circumstances (paragraph A52 of **Agenda Item 2–B**). This application material assists in emphasizing the principle of the QMA, i.e., that it is an on an ongoing and

[7] Throughout **Agenda Item 2–B** and this Agenda Item, the term "overall objective" means the objective in paragraph 16 of **Agenda Item 2–B,** while the term "quality objectives" means the quality objectives established by the firm that support the overall objective.

continuous consideration of the circumstances of the firm and modifications may be needed from time to time, as necessary. Furthermore, the results of the firm's monitoring activities may highlight deficiencies in the firm's system of quality management and paragraph 46(b) of **Agenda Item 2–B** requires the firm to consider whether such deficiencies indicate that the quality objectives are inappropriate.

65. The requirements to establish quality objectives and consider the relevance and granularity are followed by the prescribed quality objectives, which form the basis for the quality objectives to be established by the firm (paragraph 32 of **Agenda Item 2–B**).[8] The notion that the firm establishes more relevant and granular quality objectives based on these prescribed quality objectives is explained in the application material (paragraph A48 of **Agenda Item 2–B**). In identifying the prescribed quality objectives, the QCTF agreed that, consistent with the overall objective of the standard, the prescribed quality objectives would be related to:

    (a) The performance of engagements in accordance with professional standards and applicable legal and regulatory requirements.

    (b) The issuance of reports that are appropriate in the circumstances.

    Nevertheless, the QCTF noted that it is also necessary that the firm has considered the engagement acceptance and continuance. The QCTF identified two discrete aspects in relation to the engagement acceptance and continuance:

    (a) An external aspect, i.e., the integrity, ethical values or diligence of management, and, where appropriate, those charged with governance, and their competence in relation to the subject matter of the engagement.

    (b) An internal aspect, i.e., the firm has sufficient resources to perform engagements in accordance with professional standards and applicable legal and regulatory requirements.

66. As a result, the prescribed quality objectives identified by the QCTF comprise four objectives, and the QCTF is of the view that these objectives represent the minimum appropriate level of granularity.

67. The QCTF is mindful that a firm's current system of quality control is already intended to support the achievement of the overall objective. As a result, the QCTF has recommended application material to highlight that in establishing the quality objectives for the first time, the firm may identify the quality objectives based on the firm's existing system of quality control (i.e., taking into consideration the activities that are already established by the firm and determining the intended purpose of such activities) (paragraph A53 of **Agenda Item 2–B**). This point has also been included in the application material supporting the identification and assessment of risks (paragraph A58 of **Agenda Item 2–B**). The QCTF recognizes that such application material may be better placed in guidance outside of ISQC 1 and will further consider this as part of its overall evaluation of the application material and the development of supplementary guidance.

Identify and Assess Quality Risks

68. As explained above, the prescribed quality risks that would be included in ISQC 1 would be granular in order to capture the elements in extant ISQC 1 and to address the additional enhancements to ISQC 1 that were suggested in the ITC. The prescribed quality risks would not address all possible quality risks, due to the varying circumstances across firms and therefore it would be up to the firm to identify all quality risks that are relevant to the firm. The firm may also identify quality risks that are a subset of the prescribed quality risks (i.e., more granular). A further

[8] Paragraphs 78–86 below set out the QCTF's proposals on the prescribed quality objectives, quality risks and responses.

explanation of the QCTF's proposals regarding the prescribed quality risks is included in paragraphs 78–86 below.

69. In developing the requirements for the firm to identify and assess quality risks, the QCTF recognized that it would not be reasonable or practicable to expect the firm to identify and assess every possible quality risk. The QCTF agreed that there are some quality risks that are negligible and for which the firm would not be expected to take any further actions. Accordingly, the proposed requirement for the firm to identify and assess quality risks requires the firm to identify those risks that could *reasonably have an adverse* impact on the firm's ability to achieve its quality objectives. This is further explained in the supporting application material (paragraph A55 of **Agenda Item 2–B**).

70. Similar to how the risk identification and assessment process is established in ISA 315 (Revised),[9] the QCTF recommends that the risk identification be enabled through understanding the factors that could create the risks, i.e., the conditions, events, circumstances, actions or inactions that, individually or combination could adversely impact the firm's ability to achieve its objectives. Paragraph A47 of **Agenda Item 2-B** includes factors that may be useful to the firm in identifying and assessing the quality risks.

71. The QCTF noted concerns from respondents to the ITC about the risk of an error or omission at the risk assessment stage of the QMP. The QCTF is of the view that this would be addressed through the firm's reassessment of its quality risks from time to time, for example, when there are new or changes to the conditions, events, circumstances, actions or inactions that give rise to the risks or when other information comes to the attention of the firm (paragraph A57 of **Agenda Item 2-B**). Furthermore, the results of the firm's monitoring activities may highlight deficiencies in the firm's system of quality management and paragraph 46(b) of **Agenda Item 2–B** requires the firm to consider whether such deficiencies indicate that the quality risks are inappropriate. As discussed in paragraph 61, in establishing the quality objectives, the firm is required to consider the granularity of the quality objectives in order that they facilitate the identification and assessment of quality risks, which may also partially prevent an error or omission at the risk assessment stage.

72. In researching other frameworks and how the risk assessment is established, the QCTF identified various factors that are useful to consider in assessing the likelihood and impact of the quality risks. The QCTF is of the view that such guidance is useful application material to support firms in assessing the quality risks and may provide some consistency in terms of how quality risks are assessed (paragraph A59 of **Agenda Item 2-B**).

73. The QCTF noted the IAASB's suggestion in December 2016 that the firm would need to establish its risk tolerance, which is linked to obtaining a reasonable level of assurance regarding the effectiveness of its system of quality management and is consistent with the principles in the COSO Integrated Framework. The QCTF debated how this concept would be applied in establishing quality objectives and identifying and assessing risks in the firm's system of quality management, and concluded that such an approach would add too much complexity to the standard. However, the QCTF is of the view that the concept of reasonable assurance in the context of a system of quality management could be better explained in ISQC 1 and this has been incorporated in the application material supporting the definition of reasonable assurance (paragraphs A5 and A6 of **Agenda Item 2–B**).

[9] ISA 315 (Revised), *Identifying and Assessing the Risks of Material Misstatement through Understanding the Entity and Its Environment*

Design and Implement Responses to Quality Risks

74. Similar to how the quality risks would be established in ISQC 1, the prescribed responses that would be included in ISQC 1 would be granular in order to capture the elements in extant ISQC 1 and to address the additional enhancements to ISQC 1 that were suggested in the ITC. The prescribed responses would not include all possible responses that are necessary to address quality risks, due to the varying circumstances across firms and to support the notion that the system of quality management is tailored to the firm. Therefore it would be up to the firm to design and implement responses to address all quality risks, including the prescribed quality risks. A further explanation of the QCTF's proposals regarding the prescribed responses is included in paragraphs 78–86 below.

75. Consistent with any risk-based framework, the QCTF is of the view that the nature, timing and extent of the responses to the quality risks is driven by the assessment of the quality risks, i.e., the higher the assessed risk, the more rigorous the response. The response is also affected by the factors that have caused the risk, for example, if the cause is a lack of information and communication, the response would focus on implementing procedures to support obtaining or generating and communicating the necessary information.

76. The QCTF is of the view that explaining the different characteristics of responses to risks, for example, preventative versus detective activities or manual versus automated, may prompt firms to consider the most appropriate response to address the quality risks. As a result, application material has been included to explain the different characteristics of responses for the firm to consider (paragraph A67 of **Agenda Item 2-B**).

77. As with the quality objectives and quality risks, the QCTF has introduced application material to explain the circumstances when the responses may need to be reassessed (paragraph A70 of **Agenda Item 2-B**). This is in addition to the requirement in paragraph 46(b) of **Agenda Item 2–B** that requires the firm to consider whether deficiencies identified indicate that the responses to quality risks are inappropriate.

Prescribed Quality Objectives, Quality Risks and Responses

78. The QCTF debated how the proposed new requirements to establish quality objectives, identify quality risks and responses to such risks would be practically applied to the elements in extant ISQC 1. **Agenda Item 2–C** includes the QCTF's proposed prescribed quality objectives, quality risks and responses, however these are for illustrative purposes in order to obtain the IAASB's views on:

    (a) The level of granularity of the prescribed quality objectives, quality risks and responses.

    (b) How the prescribed quality objectives, quality risks and responses interrelate, including whether the categorization into elements, consistent with extant ISQC 1, should be retained.

    (c) Possible mechanisms for the presentation of the prescribed quality objectives, quality risks and responses in ISQC 1.

    The QCTF will further explore the specific aspects of the quality objectives, quality risks and responses, including how these may need to be enhanced in response to other proposals in the ITC (e.g., engagement partner performance and rewards) and present its proposals to the IAASB in September 2017.

79. As explained above, the QCTF concluded that:

    (a) The prescribed quality objectives would be established at a high level, to support the consistency with the overall objective of ISQC 1.

    (b) The prescribed quality risks and responses would be established at a granular level, in order to capture the elements in extant ISQC 1 and to address the additional enhancements to ISQC 1 that were suggested in the ITC. However, these prescribed quality risks and responses would be "incomplete", due to the varying circumstances across firms and to support the notion that the system of quality management is tailored to the firm.

80. The QCTF noted that firms may incorrectly assume that the prescribed quality risks and responses in ISQC 1 are complete, and could fail to identify additional quality risks and responses that are necessary in the circumstances of the firm. The QCTF is of the view that ISQC 1 needs to clearly signal the significance and importance of firms establishing more granular quality objectives (as necessary), identifying quality risks in the context of the circumstances of the firm, and designing and implementing responses that are relevant, appropriate and address the identified risks. The introductory paragraphs of ISQC 1 highlight this and it is mentioned in application material supporting the QMP. However, the QCTF will give further consideration as to whether additional application material may be necessary to further emphasize this concept (paragraphs 6, 7, A48 and A49 of **Agenda Item 2-B**).

81. In developing the prescribed quality risks and responses, the QCTF analyzed the requirements within the elements in extant ISQC 1 in order to determine whether they relate to quality risks or responses. In undertaking this exercise, the QCTF grappled with the distinction between requirements that should be prescribed quality risks and those that are prescribed responses to the quality risks, and the QCTF further debated how granular the prescribed quality risks would need to be. The QCTF concluded that prescribed quality risks would be derived from the cause of the risk, for example, the firm may inappropriately accept an engagement but there is an underlying factor that causes the firm to do so (e.g., a lack of information). The QCTF noted that in cases where the extant requirement is a prescribed response, a correlating quality risk should be developed related to the response (i.e., it would be inappropriate for prescribed responses to exist in ISQC 1 that do not have a correlating prescribed quality risk).

82. The QCTF debated whether the categorization of the quality objectives, quality risks and responses according to the elements should be retained. This consideration arose as the QCTF noted that in some cases similar quality risks and responses exist across the various elements, for example, the prescribed quality risks and responses in relation to compliance with relevant ethical requirements apply to the elements "relevant ethical requirements", "acceptance and continuance of client relationships and specific engagements" and "engagement performance". Similarly, the quality risks and responses in relation to human resources apply to the elements "acceptance and continuance of client relationships and specific engagements" and "engagement performance". In addition, the QCTF observed that categorization into elements could inadvertently discourage firms from considering quality risks and responses that may exist outside of these elements. The QCTF concluded that the categorization into elements may create an unnecessary obstacle for firms in properly identifying the quality risks and responses. Therefore the prescribed quality risks and responses have been combined into a single set of quality risks and responses (i.e., without categorization).

83. At this stage the QCTF is uncertain as to how the prescribed quality risks and responses should be placed in ISQC 1 in terms of:

    (a) Whether the quality risks and responses should be presented in a linear or tabular form.

(b) The appropriate placement of the quality risks and responses in ISQC 1, i.e., whether they should be placed near the requirements related to identifying and assessing quality risks and designing and implementing responses, or whether they should be placed in a separate section of the standard.

84. **Agenda Item 2-C** includes both a tabular and linear form of the prescribed quality risks and responses. The tabular form more clearly demonstrates the relationship between the prescribed quality objectives, quality risks and responses than the linear form and therefore a tabular form may be more understandable in practice. Furthermore, a tabular form may also more clearly signal those prescribed quality risks that do not have related responses in ISQC 1, or the prescribed quality risks where the prescribed responses in ISQC 1 do not fully address the prescribed quality risks, thereby emphasizing the notion that the firm identifies responses that are tailored to the firm in order to address quality risks. However, such a format is not traditionally used throughout the IAASB's International Standards and if not suitable for the standard, could instead be used as an appendix to ISQC 1 or in other supplementary guidance in order to support the implementation of the standard.

85. The QCTF also debated the appropriate placement of the prescribed quality risks and responses in ISQC 1. Paragraphs 35 and 37 of **Agenda Item 2-B** have been included as placeholders for these requirements. However, the QCTF is concerned that this placement could cause confusion with the overall requirements and application material related to identifying and assessing the risks and designing and implementing responses. On the other hand, placing the quality risks and responses in a separate section, "applying the QMP," as originally proposed by the QCTF in December 2016, is disconnected from the concepts of identifying and assessing risks and designing and implementing responses and firms may therefore overlook their responsibility to establish quality objectives, identify and assess quality risks, and design and implement responses that are tailored to the circumstances of the firm.

86. The QCTF indicated in their proposals in December 2016 that in order to emphasize the scalability of ISQC 1, the responses to quality risks that are specified in ISQC 1 would refer to responses in the more general sense, rather than "policies and procedures" which is the term used in extant ISQC 1. The QCTF explained that this would provide more flexibility for firms to consider the most appropriate response to the quality risk. The QCTF further debated this differentiation and the appropriate use of the terms "responses" and "policies and procedures." The QCTF concluded that the prescribed responses (i.e., those in **Agenda Item 2–C**) should require the firm to establish policies and procedures, as there is a need to establish a consistent response to addressing quality risks in the standard. Nevertheless, the QCTF agreed that switching the term "policies *and* procedures" to "policies *or* procedures" would emphasize some flexibility for the firm, for example, that policies are not required in all instances. The QCTF further agreed that the term "responses" should be used in relation to the actions designed and implemented by the firm to address quality risks that are additional to the prescribed responses in **Agenda Item 2–C**, as these actions could comprise a variety of forms, for example, training or assigning responsibility. The QCTF has included application material to explain this differentiation, as well as the advantages of having formal documented policies and circumstances when this may be needed (paragraphs A62–A63 of **Agenda Item 2-B**).

Matters for IAASB Consideration

9. Does the IAASB agree with the proposals of the QCTF in relation to the requirements to establish objectives, identify and assess risks and design and implement responses to the risks, set out in paragraphs 30–37 of **Agenda Item 2–B,** in particular:

(a) Does the IAASB agree with the considerations of the firm in establishing the quality objectives, i.e., (i) the alignment with the firm's governance principles, strategy, professional standards and applicable legal and regulatory requirement, (ii) whether they are relevant to the circumstances of the firm and all relevant quality objectives have been identified, and (iii) the appropriate level of granularity?

(b) Does the IAASB agree with the approach of identifying quality risks through an understanding of the conditions, events, circumstances, actions or inactions that could give rise to those risks?

(c) Does the IAASB agree with the threshold that has been established in identifying quality risks, i.e., those risks could reasonably have an adverse impact the firm's ability to achieve its quality objectives?

(d) Is the IAASB of the view that the requirements clearly set out the expectations in establishing quality objectives, identifying and assessing quality risks and designing and implementing responses and would these be able to be applied in practice?

10. The IAASB is asked to share their views in relation to the prescribed quality objectives, quality risks and responses set out in **Agenda Item 2–C**, in particular:

(a) Is the IAASB of the view that the level of granularity of the prescribed quality objectives, quality risks and responses is appropriate?

(b) Does the IAASB support the QCTF's proposal to consolidate the prescribed quality objectives, quality risks and responses, rather than place these into the categories according to the elements in extant ISQC 1?

(c) Does the IAASB have any suggestions regarding the presentation of the prescribed quality objectives, quality risks and responses and their placement in ISQC 1?

Monitoring and Remediation

87. In the ITC, it was noted that an effective system of quality control requires policies and procedures that provide for the regular assessment of the adequacy and effectiveness of that system, including a mechanism by which the system is evaluated and modified, as appropriate, when deficiencies are identified. It was further highlighted that the use of a QMA by the firm would create an opportunity to provide a stronger link to monitoring and remediation within the firm's system of quality control and would help to promote a focus on continuous improvements in quality. The ITC included various proposals in relation to monitoring and remediation, including the following:

(a) Strengthen the requirements and application material for firms to respond to all feedback in relation to quality control, including feedback from external inspection findings, as well as other quality reviews that a firm might perform.

(b) Include requirements to address actions firms should take to understand the causes of deficiencies identified by internal and external inspections and other reviews, and from other information sources.

(c) Introduce requirements to clarify the necessary actions regarding the analysis of audit deficiencies and corrective measures.

(d) Introduce requirements and application material addressing the monitoring by firm leadership of the effectiveness and appropriateness of remedial actions.

The QCTF observed that respondents were overall supportive of these proposals. A more detailed analysis of respondent's comments is included in the **Supplement to Agenda Item 2**.

88. Given the general support from respondents to the ITC for the proposals, the QCTF is of the view that the requirement to establish a monitoring process in paragraph 48 of extant ISQC 1 should be extended to establishing a monitoring and remediation process (paragraph 38 of **Agenda Item 2–B**).

89. The QCTF debated the purpose of the firm's monitoring and remediation process (paragraph 48 of extant ISQC 1) in determining possible revisions to ISQC 1. Under extant ISQC 1, the monitoring process is designed to provide "reasonable assurance that the policies and procedures relating to the system of quality control are relevant, adequate, and operating effectively". The QCTF is of the view that the monitoring process is not designed to provide the firm with reasonable assurance about the effectiveness of the procedures put in place to address the overall objective. The QCTF agreed that instead the monitoring and remediation process is designed as an evaluation of whether the firm's system of quality management is effective in providing the firm with reasonable assurance that its overall objective has been achieved. This has been captured in the revisions to ISQC 1 (paragraph 38 of **Agenda Item 2–B**).

90. In developing the requirements related to monitoring and remediation, the QCTF considered what this process would typically entail and identified the following steps:

    (a) Design monitoring activities, including the nature, scope and frequency of such activities;

    (b) Perform internal monitoring activities;

    (c) Assess the results of the monitoring activities and external inspections, in order to identify deficiencies in the firm's system of quality management;

    (d) Address deficiencies identified if there is an indication that a report may be inappropriate or that procedures were omitted during the performance of an engagement;

    (e) Determine the cause(s) of deficiencies and evaluate the effect of deficiencies;

    (f) Implement appropriate remedial action(s);

    (g) Monitor the effectiveness of the remedial actions and evaluate whether the remedial actions appropriately address deficiencies; and

    (h) Communicate matters in relation to monitoring and remediation.

91. This process has been included in the application material as the QCTF is of the view that it helps to clearly set out the requirements that follow within this section of ISQC 1 (paragraph A72 of **Agenda Item 2–B**).

Monitoring

92. The QCTF noted that the existing requirements in paragraph 48 of ISQC 1 are generally focused on inspection of engagements, and are not necessarily clear that monitoring activities over firm-wide controls are also important. Recognizing the views of respondents, including a member of the monitoring group[10], that more emphasis is needed on internal monitoring reviews of firm-wide controls, the QCTF recommends that more recognition is needed in the requirements in relation to monitoring the firm's overall system of quality management. This has been introduced through the following revisions:

[10] International Forum of Independent Audit Regulators

(a) A requirement for the firm to design and perform monitoring activities that are sufficient to provide the firm with an evaluation of the various components of the system of quality management (paragraph 39 of **Agenda Item 2–B**). This includes the identification of the components in order to remind firms that monitoring also addresses governance and firm leadership, information and communication and the QMP, including monitoring and remediation itself (i.e., the monitoring activities should also be sufficient to evaluate whether the monitoring and remediation supports the firm in achieving its overall objective).

(b) A requirement for the firm to determine the scope and frequency of the monitoring activities, that takes into consideration the firm's system of quality management (paragraph 40 of **Agenda Item 2–B**).

(c) Application material that includes examples of other types of monitoring activities (paragraph A77 of **Agenda Item 2–B**). Including other types of engagement reviews, such as peer reviews, may also give recognition to these forms of reviews as possible monitoring activities, as noted by respondents to the ITC, in particular those representing the views of SMPs and the public sector.

93. The QCTF recognizes that the nature, timing and extent of the firm's monitoring activities will vary from firm to firm, and therefore the requirements need to be clearly scalable. Nevertheless, there are circumstances when monitoring activities are usually undertaken, for example, in cases when the firm's circumstances have changed, aspects of the firm's system of quality management have changed, or the results of previous monitoring activities have identified a high number of deficiencies. Accordingly, paragraph 40 of **Agenda Item 2–B** requires the firm to determine the scope and frequency of the monitoring activities, taking into consideration these factors. This is supported by application material to explain how these factors or information may impact the scope and frequency of the monitoring activities, thereby highlighting the scalability of the requirement but at the same time ensuring the firm remains responsive to information that may indicate the need for monitoring activities to be undertaken.

94. The factors in paragraph 40 of **Agenda Item 2–B** also link to information obtained from external inspections, i.e., a possible deficiency in the firm's system of quality management identified from external inspections may indicate the need for monitoring activities to be undertaken. This further supports the notion that the firm should respond appropriately to information from external inspections.

Inspection of Completed Engagements

95. The QCTF is of the view that the firm should determine risk-based criteria that establish which engagements should be subject to inspection, since the nature and extent of engagement inspections is dependent on what is needed by the firm to support its evaluation of its system of quality management. Accordingly, a requirement has been introduced for the firm to do so, together with application material that sets out the types of factors for the firm to consider in determining the criteria (paragraph 41 and A81 of **Agenda Item 2–B**). Such an approach is beneficial in that it encourages the firm to consider all engagements, including those that may have been subject to the cyclical inspection process. For example, there may be a circumstance when the engagement was subject to inspection as it was selected as part of the firm's cyclical inspection of the engagement partner, but may need to be inspected in a following year as a result of certain attributes of the engagement.

96. The QCTF recognizes that the retention of a requirement to perform cyclical engagement inspections is necessary in supporting consistency across firms, however will further debate

whether this requirement should apply to all engagements as is the case in paragraph 48(a) of extant ISQC 1, or whether it should be amended to apply to audits of financial statements only.

97. The QCTF noted the views of respondents that improvement is needed in relation to engagement inspections to promote more substantive reviews of the quality of work on higher risk and judgmental areas, instead of a "tick-box" approach. The QCTF concurs with this view and has included various considerations in the application material in relation to the nature and extent of the procedures to be undertaken in performing the evaluation of completed engagements (paragraph A83 of **Agenda Item 2–B**).

Other Requirements in Extant ISQC 1

98. The QCTF noted paragraph 48(c) of extant ISQC 1 which indicates that those performing the engagement or the EQC review should not be involved in inspecting the engagement. The QCTF is of the view that those performing monitoring activities should have sufficient and appropriate experience, knowledge and capacity to perform the monitoring activity and should be sufficiently objective from the activity subject to monitoring. The QCTF notes that this would apply to all monitoring activities and not only those related to inspection of engagements and therefore have included this as a general requirement (paragraph 42(b) of **Agenda Item 2–B**). The extent of such experience, knowledge, capacity and objectivity would vary depending on the underlying activity being monitored and this is explained in the application material.

99. The QCTF has also retained the requirement for the firm to assign responsibility for the monitoring process to a partner or partners or other persons with sufficient and appropriate experience and authority in the firm to assume that responsibility. However, consistent with the assignment of responsibility in relation to independence, this requirement refers to assigning "operational responsibility" for monitoring and remediation (paragraph 42(a) of **Agenda Item 2–B**).

Remediation

100. The QCTF agreed that after performing the monitoring activities, it is necessary for the firm to assess the results in order to identify possible deficiencies. The QCTF also noted the general support from respondents for addressing the results of external inspections in ISQC 1. Accordingly, a new requirement for the firm to assess the results of its monitoring activities and external inspections has been introduced (paragraph 43 of **Agenda Item 2–B**). This is supported by a new definition explaining the meaning of "external inspections" to provide further clarity on the scope of inspections that should be subject to the firm's consideration (paragraph 17(i) of **Agenda Item 2–B**).

101. The QCTF observed respondents' support for introducing a causal analysis for deficiencies identified by inspections and other types of reviews. The QCTF had various debates in relation to the causal analysis and addressing the deficiencies, including:

    (a) On which deficiencies the causal analysis should be performed.

    (b) At what point the pervasiveness of the deficiency is considered (i.e., whether it is systemic or isolated), for example, when the deficiency is identified or after performing the causal analysis.

    (c) Whether the remedial actions are designed to address the deficiencies or the causes of the deficiencies, and how ISQC 1 would address remedial actions in relation to deficiencies for which no causal analysis has been performed

102. The QCTF concurred that once a deficiency has been identified in relation to an engagement and there is an indication that the report may be inappropriate or that procedures were omitted during

the performance of the engagement, the firm would be expected to take immediate action, irrespective of the cause of the deficiency. Accordingly, paragraph 44 of **Agenda Item 2–B** includes this requirement, which is similar to paragraph 52 of extant ISQC 1.

103. While deficiencies are typically identified from monitoring activities or external inspections, other information sources may also indicate deficiencies in the firm's system of quality management. Accordingly, the application material notes that deficiencies may be identified from sources other than monitoring activities and provides examples (paragraph A88 of **Agenda Item 2–B**).

Causal Analysis

104. The QCTF debated which deficiencies should be subject to a causal analysis and determined that the causes of all deficiencies should be understood by the firm in order to implement appropriate remedies. The QCTF also agreed that the nature and extent of the firm's process to determine the causes of the deficiencies would vary depending on the nature of the deficiency. For example, the causes of some deficiencies may be more obvious and immediately identifiable, whereas other deficiencies may need a more rigorous process to understand the underlying causes. As a result, a requirement for the firm to determine the causes of deficiencies has been introduced, and the nature, timing and extent of the procedures undertaken is determined by the firm based on the nature of the deficiencies (paragraph 45 of **Agenda Item 2–B**). This is supported by application material to explain that the work effort of the firm may vary according the nature of the deficiency (paragraph A90 of **Agenda Item 2–B**).

105. As a result of this resolution, the QCTF agreed that it would be inappropriate to use terminology such as "root cause analysis" and "causal factor analysis" in these requirements. The QCTF noted that these terms are commonly used in practice and are generally implied as a rigorous process established by firms to understand the causes of deficiencies. The QCTF is of the view that it would be inappropriate for firms to apply such a rigorous process to all deficiencies identified.

106. The QCTF recognizes the importance of ensuring that the breadth and depth of the causal analysis is appropriate so that the right causes are identified. Accordingly, application material has been included that explains the purpose of the causal analysis, provides examples of causes to indicate the level of specificity, and explicitly explains that the factors need to be specific with an illustration of factors that are insufficiently specific, for example, a lack of professional skepticism (paragraphs A93–A94 of **Agenda Item 2–B**).

107. Furthermore, the QCTF has introduced application material that provides an overview of some of the procedures the firm may implement in order to undertake a causal analysis (paragraph A92 of **Agenda Item 2–B**). In developing this guidance, the QCTF referred to the recent publication by the United Kingdom Financial Reporting Council, *Audit Quality Thematic Review Root Cause Analysis A review of the six largest UK audit firms*. The QCTF has also included guidance to emphasize the importance of establishing the competence of those performing the causal analysis.

Evaluating the Effect of Deficiencies

108. Paragraph 49 of extant ISQC 1 requires the firm to evaluate the effect of deficiencies. The QCTF is of the view that evaluating the effect of the deficiencies is important, as this affects the nature, timing and extent of the remedial actions. Accordingly, the requirements indicate that the firm is required to evaluate the effect of the deficiencies and further requires the firm to determine whether the causes are systemic, repetitive or other causes that require timely remedial action (paragraph 46 of **Agenda Item 2–B**).

109. The revised requirements also require the firm to consider the continued relevance of the firm's quality objectives, whether all quality risks have been identified and appropriately assessed and whether the responses to quality risks remain appropriate (paragraph 46(b) of **Agenda Item 2–B**). This is an important step in the QMP since it links back to the firm's assessment of its quality objectives, quality risks and responses.

Remedial Actions

110. The QCTF noted that paragraph 51 of extant ISQC 1 includes remedial actions that the firm is required to implement, for example, changes to policies and procedures, communication to those responsible for training etc. The QCTF is of the view that these requirements are too restrictive and do not provide flexibility for firms to identify the most appropriate and effective remedial actions. Accordingly, the QCTF has proposed removing the specific actions, and replacing them with a requirement that requires the firm to implement appropriate remedial actions (paragraph 47 of **Agenda Item 2–B**).

111. Consistent with the proposals in the ITC and as a result of the general support from respondents, the QCTF has proposed a new requirement for the firm, including those assigned ultimate responsibility and accountability for quality, to monitor the effectiveness of the remedial actions to address the causes and evaluate whether the remedial actions appropriately address the deficiencies identified (paragraph 48 of **Agenda Item 2–B**).

Communicating Matters Related to Monitoring and Remediation

112. Paragraphs 50 and 53 of extant ISQC 1 include requirements related to communication. The QCTF recommends that these be consolidated into a single requirement addressing communication with the parties identified in paragraph 28 of **Agenda Item 2–B** (paragraph 49 of **Agenda Item 2–B**). The QCTF concluded that all of these parties have some level of information needs in relation to monitoring and remediation, although these would vary depending on their roles and responsibilities. Therefore the requirement emphasizes the relevance of the information to be communicated.

113. The QCTF also debated whether the requirement to communicate on an annual basis should remain. The QCTF agreed that in some circumstances information may need to be communicated more frequently than on an annual basis in order that causes are rectified and remedial actions implemented on a timely basis. However, the QCTF is of the view that the requirement to communicate at least annually should be retained, as this would drive the firm to assess their system of quality management at least on an annual basis. Accordingly, the QCTF recommends that the requirement indicate that the information should be communicated on a timely basis or at least annually.

Matters for IAASB Consideration

11. Paragraph 14(b) discusses the QCTF's recommendation to retain monitoring and remediation as a subset of the QMP process. Does the IAASB agree with this recommendation?
12. Does the IAASB agree with the purpose of monitoring and remediation explained in paragraph 89?
13. Does the IAASB support the inclusion of external inspections in paragraph 40 and 43 of **Agenda Item 2–B**?

14. Does the IAASB consider the requirements in paragraph 40 of **Agenda Item 2–B** to be appropriate, including the factors the firm is required to consider in determining the scope and frequency of the monitoring activities?

15. Does the IAASB agree with the QCTF's recommendation in relation to engagement inspections, i.e., that the firm is required to set out criteria for the selection of completed engagements for inspection that sufficiently support the firm in its evaluation of its system of quality management?

16. Does the IAASB agree with the proposal to include a requirement relating to the experience, knowledge, capacity and objectivity of those performing the monitoring activities?

17. Does the IAASB support the proposals in relation to the causal analysis, in particular, does the IAASB agree with the conclusion of the QCTF that the causal analysis should apply to all deficiencies that are identified by the firm, and that the nature, timing and extent of the procedures undertaken by the firm to determine the cause(s) of deficiencies are determined by the firm based on the nature of the deficiencies?

18. Does the IAASB agree with including a requirement in monitoring and remediation for the firm to consider the appropriateness of the quality objectives, quality risks and responses in evaluating the effect of deficiencies identified?

19. Does the IAASB agree with the inclusion of a requirement for the firm, including those assigned ultimate responsibility and accountability for quality, to monitor the effectiveness of the remedial actions and evaluate whether they appropriately address the deficiencies identified?

20. Does the IAASB agree with the revisions to the communication in relation to monitoring and remediation, including the conclusion to retain the requirement to communicate on an annual basis?

Interconnectedness of the Components

114. The components within the system of quality management are highly interconnected. The governance principles form the framework for how the firm's decisions are made and therefore promote an environment that sustains and improves quality. The actions the firm takes to implement the governance principles may include the responses the firm designs and implements in addressing the quality risks, for example, the firm's responses in relation to compliance with relevant ethical requirements may assist the firm in embedding the firm's internal culture, in particular the professional and ethical values.

115. Information and communication is necessary in order for all of the components of the firm's system of quality management to function. There are requirements that are directly linked to information and communication, for example, in relation to monitoring and remediation. There are also numerous prescribed quality risks and responses that relate to information and communication, for example, those relating to engagement acceptance and continuance. Information also supports the firm in establishing quality objectives and identifying and assessing quality risks and in undertaking monitoring and remediation activities.

116. Establishing the quality objectives also has many relationships with the other components. For example, in establishing the quality objectives the firm's governance principles are required to be considered. Furthermore, when deficiencies in the firm's system of quality management are identified, including as a result of monitoring activities, the firm is required to consider the continued relevance of the firm's quality objectives.

117. The same requirement applies to quality risks and responses, i.e., when deficiencies in the firm's system of quality management are identified, the firm is required to consider whether the quality risks and the responses to quality risks remain appropriate.

118. In designing the monitoring activities, the firm is required to determine the scope and frequency of the monitoring activities by taking into consideration various factors that include the design and implementation of the firm's system of quality management, for example, quality risks that are assessed as higher risks may warrant increased focus in monitoring activities. Furthermore, as highlighted above, the results of the monitoring activities may also indicate deficiencies in relation to the quality objectives, quality risks and responses that require further consideration.

119. The firm's responses to quality risks may provide information that indicates deficiencies in the firm's system of quality management. For example, responses that monitor breaches of the firm's independence policies or procedures may highlight deficiencies in the firm's system of quality management.

120. The QCTF is of the view that it is important that the relationships between the various components are clear, since the components depend on the proper functioning of other components and the firm's evaluation of its system of quality management focuses on the system as a whole, rather than the individual components that make up the system. Accordingly, throughout the requirements and application material, the QCTF has explained these relationships and included various cross-references, as appropriate.

Matter for IAASB Consideration

21. The IAASB is asked to share their views regarding whether the interconnectedness of the components is clear in **Agenda Item 2–B**?

Changing Behaviors

121. In December 2016 and March 2017, both the IAASB and the CAG encouraged the QCTF to consider how the proposals would change firm behavior. The QCTF is mindful that a firm's current system of quality control is intended to support the achievement of the overall objective of ISQC 1. The QCTF further noted that behaviors are influenced by a range of factors, including factors that exist outside the system of quality management, for example, the Audit Quality framework describes some of the external factors that contribute to the improvement of audit quality.

122. The QCTF is of the view that the revisions to ISQC 1 could positively influence firm behavior and the behavior of the firm's personnel (including firm leadership and those assigned operational responsibility for the firm's system of quality management) in a variety of ways. These include the following:

    (a) A preventative approach to managing quality. The risk-based approach that has been integrated into the revisions in ISQC 1 would result in firms anticipating the risks that could arise in order to proactively implement responses to address them. Under extant ISQC 1, the policies and procedures are standardized across firms, and therefore additional risks that are specific to the firm's circumstances may not be proactively identified, considered and addressed.

    (b) A clear responsibility for the firm to consider the system of quality management on an ongoing basis. Across the proposed revisions, the firm is required to respond to information that may impact its system of quality management, for example, changes in the firm's circumstances and information that may indicate deficiencies in the firm's system of quality management. Under extant ISQC 1, there is no recognition of the impact of changes in the

firm's circumstances, or clear need to respond to information that may indicate deficiencies. Considering the system of quality management on an ongoing basis will require firm-wide efforts and a long term commitment to quality.

(c) A responsibility to tailor the system of quality management for the circumstances of the firm. The revised approach to ISQC 1 is a risk-based approach for which targeted responses are designed and implemented by the firm. While the requirements in extant ISQC 1 would be retained in the form of prescribed quality risks and responses, these are being taken a step further as the firm would be required to identify additional quality risks and consider whether additional responses are needed in the circumstances.

(d) A holistic approach to quality management. This is established through the interrelationship of the components. In extant ISQC 1 the elements are set up independently of each other and there is not a clear link as to how the outcome of a particular element impacts other aspects of the firm's system of quality control. Under the new approach, in setting up and maintaining its system of quality management, the firm would need to ensure that the components are suitably interconnected.

(e) A responsibility on the firm to embed governance principles that support quality and the firm's public interest role and enhanced responsibility and accountability of firm leadership. The new governance principles and enhanced responsibility and accountability of firm leadership are more robust than the responsibilities of firm leadership in extant ISQC 1, thereby placing additional responsibilities on firm leadership for quality. These changes include increased focus on the firm's culture and the role of firm leadership in embedding that culture through the firm. The firm's culture directly influences the behavior of all firm personnel.

(f) A responsibility to establish mechanisms to support information and communication. The proposed changes support a more robust approach to obtaining or generating and communicating information throughout the firm and emphasizes that communication is two-way. This is expected to change firm behaviors as information and communication will be a critical consideration in establishing and maintaining a system of quality management.

(g) Increased recognition of external stakeholders, to improve the firm's recognition of its public interest role. This is established in both the governance principles and in the information and communication and is expected to influence firm behavior through factoring the firm's public interest role in the decisions made by the firm and in engaging with external stakeholders.

(h) Improved understanding of the causes of deficiencies. This is established by the requirement for the firm to understand the causes of deficiencies identified, which is not a requirement in extant ISQC 1. An improved understanding of the causes of deficiencies is expected to influence firm behavior since it would assist the firm in properly addressing the causes of deficiencies.

Matter for IAASB Consideration

22. The IAASB is asked to share their views regarding how the proposals could change firm behavior, and whether there are any unintended consequences on firm behavior that may arise as a result of the proposed revisions to ISQC 1.

Separate Standard Addressing EQC Reviews

123. Given the importance and value placed on the role of the EQC review by stakeholders, particularly investors and regulators, the ITC requested views from respondents regarding whether a separate EQC review standard would be appropriate to give further prominence to, and emphasize the importance of, the EQC review. Respondents to the ITC had mixed views regarding whether a separate standard should be developed for EQC reviews.

124. The QCTF presented the views of respondents to the IAASB at the September 2016 IAASB meeting, and the IAASB agreed with the QCTF's view that the necessity for a separate standard would only be clear once the QCTF has considered all of the issues relating to EQC reviews, in particular the complexity and volume of the enhanced proposals and how these integrate within the firm's system of quality management.

125. Subsequent to the discussion with the IAASB in September 2016, the QCTF has presented the proposed requirements and application material relating to EQC reviews to the IAASB in both December 2016 and March 2017. In order to further develop the exposure draft of ISQC 1, the QCTF is of the view that it would be beneficial at this time to determine whether the requirements relating to the EQC review should be incorporated into a separate standard.

126. Both extant ISQC 1 and ISA 220[11] include requirements and application material discussing the EQC reviewer's responsibilities with respect to the performance of the EQC review (including what the review should include, the eligibility of the EQC reviewer and the documentation requirements) and such requirements are repetitive across the two standards. ISQC 1 contains requirements regarding which engagements are subject to an EQC review and paragraph 19 of ISA 220 contains requirements addressing the responsibility of the engagement partner in relation to the EQC review.

127. If a separate standard were to be developed, i.e., a new ISQC, the QCTF envisions that the requirements would be established in a manner similar to how the communication of key audit matters are established in ISA 700 (Revised)[12] and ISA 701:[13]

    (a) A requirement would remain in ISQC 1 under the responses to quality risks for the firm to establish policies or procedures that require an EQC review to be performed for audits of financial statements of listed entities, where required by law or regulation and other engagements according to the firm's risk-based criteria (for example, see R13 in **Agenda Item 2–C**). This would be supported by application material that addresses which engagements fall within the scope of an EQC review.

    (b) All other requirements related to EQC reviews would be placed in a new ISQC, i.e., the requirements related to how the EQC review should be performed, the eligibility of the EQC reviewer and the documentation of the EQC review.

128. However, if a separate standard was not developed, the QCTF envisions that all of the requirements in relation to the EQC review would remain in ISQC 1, however the location of such requirements would need to be further considered, given they would be of a different nature than the other prescribed responses proposed by the QCTF.

129. Under both options, the requirements in ISA 220 in relation to an EQC review would be those related to the responsibility of the engagement partner (similar to those contained in paragraph 19 of extant ISA 220) and the engagement partner's responsibility to implement firm level policies

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11 ISA 220, *Quality Control for an Audit of Financial Statements*

12 ISA 700 (Revised), *Forming an Opinion and Reporting on Financial Statements*

13 ISA 701, *Communicating Key Audit Matters in the Independent Auditor's Report*

or procedures at an engagement level. The requirements in paragraph 20 and 21 of extant ISA 220 would not remain.

130. The QCTF considered the various benefits and challenges of developing a separate standard or retaining the requirements in ISQC 1. The performance of an EQC review is a required response in the circumstances when the engagement meets the prescribed criteria and is addressed through requirements that prescribe the nature and extent of the EQC review and the eligibility and selection of the EQC reviewer. Therefore, the nature of these requirements are more robust in comparison to how the other required responses of ISQC 1 have been developed (i.e., the other responses often require the firm to develop policies or procedures but do not prescribe specific requirements to be contained within those policies or procedures). Further, the QCTF is of the view that the level of prescription in relation to the requirements addressing EQC reviews is inconsistent with the underlying concepts of a QMA that have been embedded in the revisions to ISQC 1. Furthermore, locating the material in a separate standard would allow for greater elaboration of the requirements and application material.

131. The QCTF also considered whether placing the requirements in a separate standard would help emphasize the scalability of ISQC 1. The QCTF concluded that this would assist with emphasizing the scalability of ISQC 1 as it may support the concept that the firm identifies the most appropriate responses to address quality risks (i.e., if the EQC review is not required to be performed or does not meet the firm's risk-based criteria, other responses may be appropriate). The QCTF is also of the view that the scalability of ISQC 1 would be clearer as the new ISQC would apply only when firms are required or choose to perform an EQC review (i.e., similar to how the communication of key audit matters is addressed in ISA 700 (Revised) and ISA 701).

132. The QCTF noted the challenges set out in the ITC regarding the development of a separate standard, in particular that this approach could result in duplication or that linkages between the EQC review and the overall system of quality management could be lost. However, the QCTF determined that a separate standard would not result in duplication or a missing linkage, given that the requirement for the performance of an EQC review would remain in ISQC 1, with the details of how this is undertaken being located in the new ISQC.

133. However, the QCTF observed that locating the requirements in a separate standard could be perceived as giving undue prominence to an EQC review in relation to other important factors in quality management, in particular the role of the engagement partner.

Matters for IAASB Consideration

23. Does the IAASB support the development of a separate standard for EQC reviews?

Next steps

134. As highlighted throughout this paper, the QCTF continues to deliberate the other discrete topics that form part of a firm's system of quality management. The table below highlights the various topics that have been discussed with the IAASB since the issuance of the ITC, including those set out in this Agenda Item, and the additional topics that have yet to be considered by the QCTF and presented to the IAASB. Following the June 2017 discussion, the QCTF will consider the next topics to be deliberated and presented to the IAASB in September 2017 and those that will be discussed at a later time.

135. The QCTF will continue to coordinate with the ISA 220 Task Force at both a Staff and Task force level, including on matters of mutual interest such as networks and client engagement acceptance and continuance. The QCTF recognizes that the changes to ISQC 1 may also impact the IAASB's

International Standards other than the ISAs, and these will need to be further considered in terms of whether conforming amendments or other changes are needed.

136. The QCTF observed that the various changes to the International Ethics Standards Board for Accountants (IESBA) *Code of Ethics for Professional Accountants* (the Code) may impact ISQC 1 and these will need to be considered in drafting the quality risks and responses. Conversely, the proposed changes to ISQC 1 may have an impact on various aspects of the IESBA Code. Accordingly, the QCTF intends on coordinating with the IESBA Staff on matters of mutual interest as the revisions to ISQC 1 are further developed.

Topic	**Discussions with the IAASB since the issuance of the ITC**	**Further discussions**
Components of ISQC 1	December 2016 and June 2017	No further discussions are likely necessary
Governance and leadership, including organization, culture and strategy	June 2017	Further discussions in response to the IAASB's input from June 2017
Information and communication	June 2017	Further discussions in response to the IAASB's input from June 2017
Documentation		To be presented to the IAASB later in 2017
Transparency reporting		To be presented to the IAASB in September 2017
QMP	June 2017	Further discussions in response to the IAASB's input from June 2017
Prescribed quality objectives, quality risks and responses	June 2017	Further discussions needed on the quality objectives, quality risks and responses and how these will be presented in ISQC 1, to be presented to the IAASB later in 2017
EQC reviews	September 2016, December 2016, March 2017 Separate standard: June 2017	Further discussions in response to the IAASB's input from March 2017 and June 2017
Engagement partner performance and rewards, and engagement partner		To be presented to the IAASB in September 2017

Topic	Discussions with the IAASB since the issuance of the ITC	Further discussions
competency and human resources		
Monitoring and remediation	June 2017	Further discussions in response to the IAASB's input from June 2017 Consideration of outstanding issue on engagement inspections to be presented to IAASB later in 2017
Networks	June 2017 (**Agenda Item 4–A**)	How this will specifically be addressed in ISQC 1 will be presented to the IAASB later in 2017
Consideration of the effect of changes to the IESBA Code		To be presented to the IAASB later in 2017
Impact on IAASB's International Standards (excluding the ISAs)		To be presented to the IAASB in early 2018

Appendix

Minutes from the December 2016 IAASB Meeting

Quality Control – ISQC 1

Ms. French provided an overview of the Quality Control Working Group's (QCWG) recommendations on the possible approach to revising ISQC 1 to incorporate quality management, as presented in **Agenda Item 6-A**. Ms. French provided feedback from the SMP Committee, highlighting its support for the proposals and the components and their agreement that the proposals would keep the standards robust. She noted, however, their concerns that the proposals could be an add-on to the existing requirements of ISQC 1 and the SMP Committee's encouragement to ensure the standards are scalable. She added that the SMP Committee encouraged the IAASB to keep the standards clear and simple, to think about the appropriate placement of the examples and to consider how the incorporation of quality management would operate in networks of firms.

The Board was supportive of the overall direction proposed by the QCWG, but emphasized the importance of the change management related to this project, including considering what the proposals are expected to achieve, how the proposals would change behaviors and the impact on audit firms, as well as how regulators inspect audit firms. The Board encouraged the QCWG to improve the linkage of ISQC 1 to the Audit Quality Framework, and to consider the applicability of the proposals to other services as the standard is developed.

COMPONENTS OF QUALITY MANAGEMENT

The Board was supportive of the proposed components of quality management and how these were depicted in the diagram to reflect how they inter-relate. The Board provided the following suggestions:

- Governance and leadership are important to the effective functioning of the firm's quality management, however "governance and leadership" are elements that exist outside of the firm's quality management and should be articulated in terms of the role they play in the firm's quality management.
- "Organization, culture and strategy that foster quality" should be presented as a separate component from "governance and leadership", as this is a fundamental element of quality management that could be understated if it were subsumed as part of "governance and leadership". Furthermore, the link between "governance and leadership" and "organization, culture and strategy that foster quality" needs to be clear, as well as any relationship between firm culture and ethical considerations.
- Given the fundamental nature of "monitoring and remediation", it may warrant more prominence than how it is depicted or implied in **Agenda Item 6-A**.
- "Information, communication and documentation" are not foundational components for effective quality management, but are rather important measures needed to support effective quality management. Furthermore, documentation is conceptually a subset of information and communication and accordingly should not be incorporated in the heading.
- The difference between "quality management" and the "QMP" needs to be clarified, as well as what is considered to be components of quality management and elements of applying the QMP. Clarification of other terminology was also recommended and there were some suggestions to align the terminology with that used in the COSO Integrated Framework.

ROBUSTNESS OF ISQC 1

The Board was of the view that more specific details of how the proposals would be developed is necessary to support the understanding of whether the robustness of ISQC 1 would be retained. The Board also recommended that the requirements be established in terms of levels, through establishing outcomes-based or principles-based requirements at an overall level, providing flexibility in terms of their implementation, with a further layer of more specific requirements.

SCALABILITY OF ISQC 1

The Board agreed with the QCWG's suggestions on how to incorporate scalability in ISQC 1, and provided the following additional comments and questions:

- What is meant by "scalability" and "proportionality" needs to be clarified in order to facilitate the development of the requirements.
- How the concepts of quality management would apply in the circumstance of networks of firms is important to being able to demonstrate scalability.
- Being clear about at what level the "QMP" would be applied within the firm, including whether it applies to all services, would be necessary to establishing the scalability of ISQC 1.
- The use of terminology is important, for example, "informal" has connotations that the firm does not need to have very rigorous quality management and would be better contextualized as "simple."

QUALITY MANAGEMENT PROCESS

The Board noted that this would be an area that would be particularly challenging for SMPs to implement. The Board also had various suggestions relating to the proposals in respect of the requirements for the QMP:

- With respect to the assessment of the risks to quality, the Board cautioned that this should not be confused with performing the assessment of risks of material misstatement as contemplated in ISA 315 (Revised), and the assessment should be based on an understanding of the engagements performed by the firm.
- Consistent with the COSO Integrated Framework, the firm would need to establish its risk tolerance, linked to obtaining a reasonable level of assurance regarding the effectiveness of its quality management.
- There should be recognition in ISQC 1 that responses to quality risks may be established by the firm but are implemented at an engagement level.
- It was suggested that "re-evaluating the QMP" should not be a discrete element, and that this would be part of monitoring and remediation and the assessment by firm leadership of the effectiveness of the firm's quality management.

APPLYING THE QUALITY MANAGEMENT PROCESS

The Board did not agree with the use of the phrase "at a minimum" to indicate that the objectives and responses are the minimum required in addition to the firm's own evaluation of its quality objectives and responses, as it was perceived that this could create unintended consequences. The Board encouraged the QCWG to establish well-defined objectives that clarify what is considered to be quality. The Board recommended that the identification and assessment of risks to quality also needs to be included in order to support the requirement being scalable and proportional and that the term

"responses" be considered in the context of other control frameworks and the terminology in the ISAs. The Board cautioned that the existing requirements of ISQC 1 would need to be carefully considered as they are updated and transposed.

PIOB OBSERVER REMARKS

Prof. Van Hulle highlighted the importance to the public interest of establishing requirements that support consistent audit quality across firms globally.

WAY FORWARD

The QCWG will consider the Board's comments in further developing the revisions to ISQC 1, as well as considering what outreach will be necessary in 2017 in order to establish how the proposals may impact firms and regulators. The QCWG will present their further recommendations to the Board at its March 2017 meeting, in particular in relation to monitoring and remediation, governance and leadership and information, communication and documentation.

Extract of Minutes from the March 2017 CAG Meeting

Ms. French introduced the topic and explained how a QMA would be translated into the various components comprising the firm's system of quality management. She further indicated how the structure of ISQC 1 would be revised to accommodate these components and explained how the existing elements of ISQC 1 would be adapted to reflect the principles of quality management. Ms. French provided insight as to how the QCTF envisions the robustness of the requirements of ISQC 1 would be retained, while at the same enhancing the scalability of the standard.

The Representatives were generally supportive of the direction proposed by the QCTF in relation to how a QMA would be incorporated in ISQC 1 and the proposed components. The Representatives commented further as follows:

- Mr. Iinuma and Mr. James were of the view that more clarity is needed on how these proposals would be operationalized, including scalability. Mr. James was also unclear as to whether a QMA is "built-in" to ISQC 1 or whether it would be an "add-on" to ISQC 1. Ms. French agreed that it is difficult to understand the proposals until such time as all of the requirements are presented together and noted that this would be the focus of the QCTF in the next few months.
- Mr. Baumann suggested clearly articulating the problems with the extant standard and evaluating how the QMA would solve these problems, for example, if there are consistently high levels of deficiencies in the audits performed, how would improvements to the firm's system of quality control translate into improvements in the quality of audits. Mr. Iinuma was of the view that examples of where firms have applied a QMA in practice would be helpful and also questioned how a QMA would change firms` behaviors. Ms. French agreed that as the standard is developed, it will be critical to keep in mind the original intention of the changes. She added that practical examples will be critical to proving the concept of a QMA, including demonstrating the scalability of ISQC 1 and how firms of different sizes would apply the requirements.
- Ms. Pettersson agreed with Mr. Bauman's comments and questioned whether a QMA would promote and support a more preventative and continuous approach to quality management, i.e., that quality is achieved in the engagement throughout the process, rather than quality being addressed through detection at the end or after the completion of the engagement. Prof. Schilder agreed and noted that achieving quality the first time around is the fundamental goal. Ms. French noted that the foundations of the QMA are based on a preventative, proactive

approach to quality management, rather than a detective approach, and highlighted that the revisions to ISA 220 would also incorporate this principle.

- Messrs. Perera and Lang were supportive of the proposals relating to scalability. However, Ms. Molyneux cautioned that overly emphasizing scalability could result in firms not implementing policies and procedures, or other responses, necessary to comply with ISQC 1 and that adequately address the firm's responsibility for quality. Similarly, Mr. Yoshii noted that in practice entities may appoint firms without appropriate resources and skills because the audit fees are lower for such firms. Mr. James was of the view that while flexibility is positive, the standard also needs to enable consistent application in practice and be enforceable. Ms. French explained that maintaining the robustness of the standard is critical to the revisions, and that there would be certain objectives, risks and responses which all firms would be expected to apply that are based on the current elements of ISQC 1.
- Mr. Fortin was supportive of the "foundational components" as important aspects that underpin the firm's system of quality management. He also suggested reconsidering the term "applying the QMP", since "applying" a process is illogical and may not be sufficiently clear that this component includes requirements. Ms. French agreed that the terminology used needs to be sufficiently clear that this component incorporates requirements, and accordingly indicated that the QCTF would reconsider the terminology.
- Mr. van der Ende expressed his support for maintaining the robustness of the standard and noted that the components of governance and leadership and information and communication are very important. He explained that in the Netherlands firms are required to establish a "public interest committee" comprising external senior representatives, and that this function has resulted in a positive effect on firms through the committee's independent challenge of the firm's leadership and actions they take. Ms. French thanked Mr. van der Ende for the insightful information.
- Ms. Pettersson emphasized the importance of incorporating inspection findings into ISQC 1 in order to improve quality management.

GOVERNANCE AND LEADERSHIP, INCLUDING ORGANIZATION, CULTURE AND STRATEGY

Ms. French explained how governance principles would be introduced in to ISQC 1 and the QCTF's initial thinking regarding possible enhancements to the requirements addressing leadership's responsibilities. She added that these provisions would also address the organization, culture and strategy of the firm. Ms. French noted that the QCTF is considering including references to the firm's public interest role in the requirements and application material, where relevant, to remind firms of their responsibilities.

The Representatives were generally supportive of the QCTF's proposals in relation to governance and leadership and commented further as follows:

- Ms. Molyneux was particularly supportive of the component of "governance and leadership" and suggested that merely calling this component "governance" would encompass all of the aspects including leadership, culture, strategy and organization. Ms. French noted that the QCTF had extensively debated the terminology of the components and would consider this suggestion while ensuring the terminology is clear and understandable.
- Mr. Fortin and Ms. Molyneux noted that each individual within the firm is responsible for their work. Nevertheless, they, in addition to Mr. James and Mr. Rockwell agreed that there needs to be ultimate responsibility and accountability for quality at the highest level within the firm.

Ms. Molyneux suggested that the proposals relating to firm leadership's accountability for quality needs additional emphasis.

- Mr. Iinuma and Ms. Molyneux highlighted the importance of the governance principles being principles-based in order that smaller firms are able to apply the governance principles in practice. Ms. Robert and Ms. Lang expressed their support regarding the new QMA approach, but expressed concern that there may be difficulties for small- and medium sized practices in applying governance principles. Mr. Iinuma made reference to the Japanese audit firm governance code which is principles-based and noted that how the firms are governed would vary from firm to firm. Ms. French explained that the QCTF is considering how to develop the governance principles in a manner that would facilitate application by all firms, but at the same time ensure the requirements are not too broad that they are not sufficiently robust and achieve their intended purpose.
- Mr. James challenged the proposals of the QCTF related to the firm identifying appropriate personnel within firm leadership to be responsible and accountable for independence matters. He noted that Agenda Item H.1 suggested that firm leadership would be responsible for quality, yet it was implied that it is not possible to assign responsibility for independence to a single person. Mr. James suggested that the same principle should be applied to assigning responsibility for independence as was applied to assigning responsibility for quality to firm leadership. Ms. French explained that the QCTF was of the view that independence is subsumed as part of quality and noted that the QCTF is debating the extent to which ISQC 1 should require specific allocation of responsibility for certain matters, such as independence. Mr. James added that while he agrees that independence is a subset of quality, independence is a matter that is sufficiently important that it warrants separate identification.
- Mr. Fortin agreed that governance is an important underpinning component. However, he was concerned that the types of principles identified in Agenda Item H.1 are incomplete or limited, for example, it doesn't include a concept similar to the "public interest committee" that is required in the Netherlands and he questioned how transparency would be addressed in these principles. Ms. French explained that the QCTF had undertaken extensive research of various governance codes and other publications related to governance in developing the proposals and further explained that the topic of transparency reporting would be discussed by the QCTF and with the Board in the near future.
- Mr. Rockwell noted his support for including references to public interest in the requirements and application material.
- Mr. Yoshii noted that a culture that promotes professional skepticism at engagement level is established through the governance of the firm.

INFORMATION AND COMMUNICATION

Ms. French explained why information and communication are important to the functioning of the firm's system of quality management and further noted that the QCTF is considering how to reflect the iterative nature of information and the importance of two-way communication in the requirements. She noted that the QCTF had not yet deliberated "documentation", as further understanding is needed on how the rest of ISQC 1 would be developed.

The Representatives commented as follows:

- Mr. Yoshii noted that communication with parties external to the firm is very important. Ms. French agreed and noted that the QCTF was evaluating how to emphasize the importance of external communication in ISQC 1.

- Ms. Molyneux explained the importance of the firm communicating externally regarding the firm's governance and how it manages quality, and noted that only providing internal communication of these matters is too limited. Ms. Molyneux and Ms. Robert were of the view that such information is important to those charged with governance in appointing the audit firm and understanding their approaches to quality. Mr. James noted the International Organization of Securities Commissions report on *Transparency of Firms that Audit Public Companies*, and highlighted that firms tend to use transparency reports as a tool for marketing purposes, with inadequate information about the firm's system of quality management and how quality is being addressed and monitored. Mr. James further noted that the requirements related to transparency reports across jurisdictions are basic and therefore suggested that the IAASB has the opportunity to raise the bar by introducing requirements that promote high quality transparency reports. Ms. Molyneux agreed and added that governance is about striving to exceed the minimum requirements. Ms. French indicated that the QCTF is still considering the topic of transparency reporting and that they would consider what type of information is appropriate in developing the requirements. She added that ISQC 1 would most likely address circumstances when the firm is required to prepare a transparency report and would include the type of information that should be communicated in such circumstances.
- Mr. Baumann explained that in some jurisdictions, such as the United Kingdom, firms are required to conclude in the transparency report on the effectiveness of their system of quality control. However, he noted that often firms may conclude in the transparency report that the firm's system of quality control is effective, yet the results of external inspections reflect a different outcome. He added that companies are expected to go through a rigorous process in order to be able to conclude on the effectiveness of their internal control (e.g., in the United States) and therefore questioned whether firms should also be expected to go through a similar process in concluding on the effectiveness of their system of quality control. Mr. Fortin noted that the European Union has the same regulation as the United Kingdom.
- Mr Dalkin noted that many firms strive to undertake quality work and follow the requirements of the standards, and cautioned that adding additional requirements may disproportionately burden such firms because there are other firms that do not intend on complying with the standards. Mr. Koktvedgaard noted that through his role in relation to disciplinary hearings, firms have either failed to read the standard or have no desire to comply with the standard. Mr. Koktvedgaard was therefore supportive of less, but more precise, requirements.
- Mr. Yoshii highlighted that in Japan the quality of the transparency reports is very poor and that investors struggle to understand the information presented. Accordingly, he was supportive of the IAASB addressing this topic.
- Ms. Robert referred to the legislation within the European Union regarding the transparency report and to the Accountancy Europe publication about audit quality indicators.
- Ms. Lang indicated that the development of the requirements related to documentation would be critical to the scalability of ISQC 1.

QUALITY MANAGEMENT PROCESS

Ms. French explained how the requirements related to the QMP would be developed.

Ms. Lang noted that the Representatives were overall supportive of the direction proposed. The Representatives commented further as follows:

- Mr. Rockwell supported the concept of establishing a threshold for the risks for which no further response or consideration is needed by the firm, although was agnostic about how such a threshold should be established.
- Ms. Molyneaux indicated that those charged with governance of the entity may be interested about the quality objectives, the key performance indicators on the quality objectives, and encouraged transparency about the threshold for the risks for which no further response or consideration is needed by the firm.

The purpose of this document is to demonstrate the proposals of the Quality Control Task Force in the context of adopting a quality management approach in ISQC 1. The proposed requirements and application material set out below will be further refined once the Board has provided views on the proposed direction.

QUALITY MANAGEMENT (FIRM LEVEL) WORKING DRAFT:

INTERNATIONAL STANDARD ON QUALITY CONTROL 1 (REVISED)

QUALITY MANAGEMENT FOR FIRMS THAT PERFORM AUDITS AND REVIEWS OF FINANCIAL STATEMENTS, AND OTHER ASSURANCE AND RELATED SERVICES ENGAGEMENTS

(Effective as of December 15, 20XX)

[CONTENTS PAGE TO BE INSERTED]

Introduction

Scope of this ISQC

1. This International Standard on Quality Control (ISQC) deals with a firm's responsibilities for its system of quality management and applies to all firms of professional accountants who perform audits and reviews of financial statements, and other assurance and related services engagements. This ISQC sets forth requirements and guidance for the design, implementation and operation of the firm's system of quality management.

2. Other pronouncements of the International Auditing and Assurance Standards Board (IAASB) set out additional standards and guidance on the responsibilities of firm personnel regarding quality management for specific types of engagements. ISA 220,[1] for example, deals with quality management for audits of financial statements. Law, regulation or relevant ethical requirements may also establish additional responsibilities for the firm in relation to quality management beyond those described in this ISQC.

The Firm's System of Quality Management

3. A firm's system of quality management supports the firm in complying with professional standards and applicable legal and regulatory requirements and issuing reports that are appropriate in the circumstances. A firm's system of quality management comprises the following components:

   (a) Governance and leadership, including the organization, culture and strategy of the firm. (Ref. Para A1)

   (b) Information and communication, together with documentation of the firm's system of quality management. (Ref. Para A2)

   (c) The quality management process, which is the process by which the firm establishes its quality objectives, identifies and assesses quality risks to meeting those objectives, designs and

[1] International Standard on Auditing (ISA) 220, *Quality Control for an Audit of Financial Statements*

implements responses to those quality risks, monitors its system of quality management and implements remedial actions to address identified deficiencies. (Ref. Para A3–A4)

4. In order for the system of quality management to properly function, these components operate in conjunction with each other and are interrelated to form the system of quality management.

5. This ISQC establishes governance principles in relation to quality that provide the basis for the design, implementation and operation of the firm's system of quality management. The firm is required to implement actions to address these principles, which include the culture of the firm, the responsibility and accountability of firm leadership, the organization of the firm and the firm's consideration of its stakeholders. (Ref. Para A1)

6. The quality management process assists the firm in tailoring the system of quality management according to the circumstances of the firm, through establishing quality objectives that are specific to the firm and identifying the risks that, individually or in combination, may adversely affect the firm's ability to achieve its quality objectives. This enables the firm to design and implement responses that are responsive to the quality risks, thereby promoting the effective use of the firm's resources and the effective management of quality. Factors that may affect the firm's system of quality management include, for example, the size and operating characteristics of the firm and whether it is part of a network, the types of services the firm provides, the industries in which it operates, or the nature of the entities to which those services are provided. (Ref. Para A3–A4)

7. This ISQC includes quality objectives that form the basis for the quality objectives established by the firm, i.e., the firm identifies specific quality objectives relevant to the firm's circumstances, based on the quality objectives set out in the standard. The firm identifies quality risks in relation to such quality objectives, including the quality risks set out in this ISQC that are relevant to all firms. Furthermore, this ISQC includes responses that firms are required to implement to address the quality risks set out in this standard, however such responses may not fully address the quality risks, including due to the circumstances of the firm, and the firm may need to design and implement additional responses. (Ref. Para A4)

8. Quality management is a continuous, dynamic process that involves an ongoing consideration of the relevance and appropriateness of the firm's system of quality management. Changes in the circumstances affecting the firm (e.g., the types of services the firm provides or the nature of the entities to which those services are provided) or other information (e.g., the results of the firm's monitoring activities or information received through the firm's whistleblowing program) may indicate the need for the firm to consider the continued relevance and appropriateness of its system of quality management and modify it, as necessary.

Authority of this ISQC

9. This ISQC applies to all firms of professional accountants in respect of audits and reviews of financial statements, and other assurance and related services engagements.

10. This ISQC contains the objective of the firm in following the ISQC, and requirements designed to enable the firm to meet that stated objective. In addition, it contains related guidance in the form of application and other explanatory material, as discussed further in paragraph 13, and introductory material that provides context relevant to a proper understanding of the ISQC, and definitions.

11. The objective provides the context in which the requirements of this ISQC are set, and is intended to assist the firm in:

- Understanding what needs to be accomplished; and
- Determining what needs to be done to achieve the objective.

12. The requirements of this ISQC are expressed using "shall."

13. Where 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 may be appropriate in the circumstances.

    While 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 ISQC. Where appropriate, additional considerations specific to public sector audit organizations or smaller firms are included within the application and other explanatory material. These additional considerations assist in the application of the requirements in this ISQC. They do not, however, limit or reduce the responsibility of the firm to apply and comply with the requirements in this ISQC.

14. This ISQC includes, under the heading "Definitions," a description of the meanings attributed to certain terms for purposes of this ISQC. These are provided to assist in the consistent application and interpretation of this ISQC, 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 Control, Auditing, Review, Other Assurance, and Related Services Pronouncements* published by IFAC includes the terms defined in this ISQC. It also includes descriptions of other terms found in this ISQC to assist in common and consistent interpretation and translation.

Effective Date

15. Systems of quality management in compliance with this ISQC are required to be established by December 15, 20XX.

Objective

16. The objective of the firm is to establish and maintain a system of quality management to provide the firm with reasonable assurance that:

    (a) The firm and its personnel comply with professional standards and applicable legal and regulatory requirements; and

    (b) Reports issued by the firm or engagement partners are appropriate in the circumstances.

Definitions

17. In this ISQC, the following terms have the meanings attributed below:

    (a) Causal analysis – A process for identifying the underlying cause(s) of an identified deficiency, in order that the underlying cause(s) can be appropriately addressed by the firm.

    (b) Date of report – The date selected by the practitioner to date the report.

    (c) Deficiency in the firm's system of quality management – [Placeholder for further consideration]

(d) 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).

(e) Engagement partner[2] – The partner or other person in 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 required, has the appropriate authority from a professional, legal or regulatory body.

(f) Engagement quality control review – [To be updated]

(g) Engagement quality control reviewer – [To be updated]

(h) Engagement team – All partners and staff performing the engagement, and any individuals engaged by the firm or a network firm who perform procedures on the engagement. This excludes an auditor's external expert engaged by the firm or by a network firm. The term "engagement team" also excludes individuals within the client's internal audit function who provide direct assistance on an audit engagement when the external auditor complies with the requirements of ISA 610 (Revised 2013).[3]

(i) External inspections – Inspections of the firm's system of quality management or engagements performed by the firm that are undertaken by an external oversight authority.

(j) Firm – A sole practitioner, partnership or corporation or other entity of professional accountants.

(k) 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.

(l) Monitoring – A process comprising ongoing and periodic evaluations of whether the firm's system of quality management provides the firm with reasonable assurance that its overall objectives have been achieved.

(m) Network firm – A firm or entity that belongs to a network.

(n) Network[4] – A larger structure:

  (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 control policies and procedures, common business strategy, the use of a common brand name, or a significant part of professional resources.

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2 "Engagement partner," "partner," and "firm" should be read as referring to their public sector equivalents where relevant.

3 ISA 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 assistances is restricted to situations where it is permitted.

4 As defined in the Independent Ethics Standards Board for Accountants (IESBA) *International Code of Ethics for Professional Accountants* (Code)

(o) Partner – Any individual with authority to bind the firm with respect to the performance of a professional services engagement.

(p) Personnel – Partners and staff. [To be considered as "staff" includes only professional staff]

(q) Professional standards – IAASB Engagement Standards, as defined in the IAASB's *Preface to the International Quality Control, Auditing, Review, Other Assurance and Related Services Pronouncements*, and relevant ethical requirements.

(r) Quality objectives – The objectives established by the firm to achieve the firm's overall objective for the firm's system of quality management.

(s) Quality risk – A risk that, individually or in combination, could reasonably have an adverse impact on the firm's ability to achieve its quality objectives. [To be further considered in conjunction with the ISA 220 Task Force]

(t) Reasonable assurance – In the context of this ISQC, a high, but not absolute, level of assurance. (Ref. Para A5–A6)

(u) Relevant ethical requirements – [To be considered in the context of the IESBA's Restructure Project and whether for purposes of ISQC 1 this should relate to all staff] Ethical requirements to which the engagement team and engagement quality control reviewer are subject, which ordinarily comprise Parts A and B of the IESBA Code together with national requirements that are more restrictive.

(v) Remediation – Corrective actions implemented by the firm to address deficiencies identified in the firm's system of quality management.

(w) Response – The firm's actions to address a quality risk, including policies or procedures.

(x) Staff – Professionals, other than partners, including any experts the firm employs.

(y) Suitably qualified external person – [To be considered in context of how this term has been proposed in relation to engagement quality control reviews, i.e., the engagement quality control reviewer does not need to have the competence and capabilities to act as engagement partner] An individual outside the firm with the competence and capabilities to act as an engagement partner, for example, a partner of another firm, or an employee (with appropriate experience) of either a professional accountancy body whose members may perform audits and reviews of historical financial information, or other assurance or related services engagements, or of an organization that provides relevant quality control services.

Requirements

Applying, and Complying with, Relevant Requirements

18. Those assigned ultimate responsibility and accountability for quality, and person(s) within the firm with operational responsibility for the firm's system of quality management, shall have an understanding of the entire text of this ISQC, including its application and other explanatory material, to understand its objective and to apply its requirements properly.

[Paragraphs 19 and 20 below to be further considered in order to clearly address what is required for all firms and the areas of scalability]

19. The firm shall comply with each requirement of this ISQC unless, in the circumstances of the firm, the requirement is not relevant to the firm. (Ref: Para. A7)

20. The requirements are designed to enable the firm to achieve the objective stated in this ISQC. The proper application of the requirements is therefore expected to provide a sufficient basis for the achievement of the objective.

System of Quality Management

21. The firm shall establish and maintain a system of quality management that includes the following components:

    (a) Governance and leadership, including the organization, culture and strategy of the firm.

    (b) Information, communication and documentation.

    (c) A quality management process, that comprises:

        (i) Establishing quality objectives.

        (ii) Identifying and assessing quality risks.

        (iii) Designing and implementing responses to quality risks.

        (iv) Monitoring and remediation.

Governance and Leadership, including Organization, Culture and Strategy

22. The firm shall establish governance principles in relation to quality and implement them through actions set out in this ISQC, and other actions as appropriate. Such governance principles shall include: (Ref. Para A8–A11)

    (a) The firm's internal culture fosters quality, including professional and ethical values, to support the firm's public interest role; (Ref. Para A12–A15)

    (b) The firm is organized in a manner that supports the effective design, implementation and operation of the firm's system of quality management; (Ref. Para A16–A18, A21)

    (c) The firm has effective leadership with responsibility and accountability for quality; and (Ref. Para A19–A20)

    (d) The firm enhances stakeholder confidence in the public interest aspects of the firm's decision-making in relation to quality. (Ref. Para A26–A27)

23. The firm shall assign ultimate responsibility and accountability for quality to the firm's chief executive officer (or equivalent) or the firm's managing board of partners (or equivalent). The person(s) assuming such responsibility and accountability shall have sufficient and appropriate experience, knowledge and capacity to assume that responsibility and: (Ref: Para. A19–A20)

    (a) Conduct themselves in a manner that promotes an internal culture that fosters quality, including professional and ethical values, to support the firm's public interest role, and take actions to establish and extend that culture throughout the firm; (Ref: Para. A12–A13)

    (b) Establish a business strategy that reflects the professional and ethical values of the firm, recognizes the need for the firm to achieve quality in all engagements, supports the firm's public

interest role and recognizes that commercial considerations do not override the quality of work performed; (Ref: Para. A14)

(c) Establish an organizational structure that supports the effective design, implementation and operation of the firm's system of quality management; (Ref: Para. A16–A18, A21)

(d) Establish the necessary resources to support the design, implementation and operation of the firm's system of quality management and allocate these appropriately; and (Ref: Para. A24–A25)

(e) Promote the consideration of the interests and expectations of all stakeholders in formulating decisions in relation to quality. (Ref: Para. A26–A27)

24. Any person(s) that are assigned operational responsibility for the firm's system of quality management shall also have sufficient and appropriate experience, knowledge and capacity to assume that responsibility. (Ref: Para. A22–A23)

25. The firm shall establish periodic performance evaluations that assess the effectiveness of:

(a) The person(s) that are assigned ultimate responsibility or accountability for quality; and

(b) Any person(s) that are assigned operational responsibility for the firm's system of quality management.

The firm shall implement corrective actions to address performance issues that are identified through performance evaluations and which may affect the firm's achievement of its quality objectives. (Ref: Para. A11, A28–A29)

Whistleblowing

26. The firm shall establish policies or procedures that: (Ref: Para. A30–A33)

(a) Enable reporting, without fear of reprisal, of concerns in relation to the commitment to quality of the firm or its personnel; and

(b) Enable the investigation of concerns raised by the firm, its personnel or external parties.

27. If during the investigations into concerns, deficiencies in the design, implementation or operation of the firm's system of quality management are identified, the firm shall determine and evaluate the cause(s) of the deficiencies and implement remedial actions. (Ref: Para. A34–A35)

Information, Communication and Documentation

Information and Communication

28. The firm shall obtain, or generate, and communicate appropriate information necessary to enable and support the proper functioning of the firm's system of quality management, including information: (Ref: Para. A36–A37, A42, A45 and A46)

(a) In relation to the firm's system of quality management that is relevant to engagement teams, in order that engagement teams have the information necessary to perform the engagement; (Ref Para. A38)

(b) That is relevant to personnel performing functions in relation to the operation of the firm's system of quality management, in order that such personnel are able to fulfill their

responsibilities in relation to such roles, including those who are ultimately responsible and accountable for quality; and (Ref: Para. A39–A40)

(c) Exchanged with parties that are external to the firm. (Ref: Para. A41)

In doing so, the firm shall establish policies or procedures that facilitate the communication of such information with relevant parties that enables the firm and relevant parties to take appropriate and timely action in relation to such information. (Ref: Para. A43–A44)

Documentation

29. [Placeholder – section to be further developed]

Quality Management Process (Ref: Para. A47)

Establish Quality Objectives

30. The firm shall establish quality objectives necessary to achieve the overall objective of the firm's system of quality management. (Ref: Para. A48, A52 and A53)

31. In establishing the quality objectives the firm shall consider whether:

(a) The quality objectives are aligned with the firm's governance principles and strategy, professional standards and applicable legal and regulatory requirements; (Ref: Para. A50)

(b) The quality objectives are relevant to the circumstances of the firm and all relevant quality objectives have been identified; and (Ref: Para. A51–A52)

(c) The quality objectives are set at an appropriate level of granularity that enables the firm to identify and assess the quality risks. (Ref: Para. A49)

32. The quality objectives established by the firm shall be based on the following: [Also see **Agenda Item 2–C**]

(a) The firm accepts and continues client relationships and specific engagements for which the firm is satisfied with the integrity, ethical values or diligence of management, and, where appropriate, those charged with governance, and their competence in relation to the subject matter of the engagement.

(b) The firm accepts and continues client relationships and specific engagements for which the firm has sufficient resources to perform engagements in accordance with professional standards and applicable legal and regulatory requirements.

(c) The firm performs engagements in accordance with professional standards and applicable legal and regulatory requirements.

(d) Reports issued by the firm or engagement partners are appropriate in the circumstances.

Perform Quality Risk Assessment

33. The firm shall identify quality risks, through understanding the conditions, events, circumstances, actions or inactions that, individually or in combination, could reasonably have an adverse impact on the firm's ability to achieve its quality objectives. (Ref: Para. A54–A58)

34. The firm shall assess the likelihood and impact of the quality risks identified in paragraph 33. (Ref: Para. A59)

35. The quality risks shall include the following: [Placeholder for the quality risks – see **Agenda Item 2–C**]

Design and Implement Responses to Quality Risks

36. Taking into account the assessed likelihood and impact of the quality risks, the firm shall design and implement responses for which the nature, timing and extent are responsive to the conditions, events, circumstances, actions or inactions that gave rise to the quality risk. (Ref: Para. A60–A70)

37. The responses shall include the following: [Placeholder for the responses – see **Agenda Item 2–C**]

Monitoring and Remediation

Establishing a Monitoring and Remediation Process

38. The firm shall establish a monitoring and remediation process in order to evaluate whether the firm's system of quality management provides the firm with reasonable assurance that its overall objective has been achieved. (Ref: Para. A71–A72)

Monitoring the Firm's System of Quality Management

39. The firm shall design and perform monitoring activities that are sufficient to provide the firm with an evaluation of whether the system of quality management provides the firm with reasonable assurance that the overall objective has been achieved, including whether: (Ref: Para. A73)

    (a) The governance principles in relation to quality have been implemented and the firm's leadership has assumed ultimate responsibility and accountability for quality;

    (b) The firm's information and communication policies or procedures enable and support the proper functioning of the firm's system of quality management;

    (c) The quality management process of the firm includes appropriate quality objectives and is appropriately identifying, assessing, and responding to the quality risks; and

    (d) The firm's monitoring and remediation appropriately enable the evaluation of the firm's system of quality management.

40. The firm shall determine the scope and frequency of the monitoring activities, taking into consideration: (Ref: Para. A74–A80)

    (a) The design and implementation of the firm's system of quality management;

    (b) Changes in factors that have impacted the firm's system of quality management;

    (c) The results of previous monitoring activities and remedial actions, including whether the previous monitoring activities continue to be relevant in evaluating the firm's system of quality management; and

    (d) Other information that may suggest deficiencies exist in the firm's system of quality management, including information from external inspections that may indicate the need for the firm to conduct monitoring activities.

41. As part of the monitoring activities, the firm shall establish policies or procedures requiring the inspection of completed engagements. Such policies or procedures shall set out criteria for the selection of completed engagements for inspection that sufficiently support the firm in its evaluation of its system of quality management. Such criteria shall include the inspection of at least one completed engagement for each engagement partner on a cyclical basis determined by the firm. (Ref: Para. A81–A83)

42. The firm shall:

    (a) Assign operational responsibility for the monitoring process to a partner or partners or other persons with sufficient and appropriate experience and authority in the firm to assume that responsibility; and

    (b) Determine that those performing the monitoring activities have sufficient and appropriate experience, knowledge and capacity to perform the monitoring activity and are sufficiently objective from the activity subject to monitoring. (Ref: Para. A84–A85)

Identifying and Remediating Identified Deficiencies

43. The firm shall assess the results of the monitoring activities and external inspections, in order to: (Ref: Para. A86–A88)

    (a) Identify deficiencies in the firm's system of quality management;

    (b) Determine the cause of deficiencies and evaluate their effect; and

    (c) Implement appropriate remedial actions.

44. In circumstances when a deficiency identified relates to an engagement and there is an indication that the report may be inappropriate or that procedures were omitted during the performance of the engagement, the firm shall:

    (a) Determine what further action is necessary to comply with relevant professional standards and applicable legal and regulatory requirements; and

    (b) Consider whether to obtain legal advice.

45. The firm shall determine the cause(s) of deficiencies. The nature, timing and extent of the procedures undertaken by the firm to determine the cause(s) of deficiencies shall be determined by the firm based on the nature of the deficiencies. (Ref: Para. A89–A94)

46. The firm shall evaluate the effect(s) of deficiencies, taking into account the identified cause(s). In doing so the firm shall:

    (a) Determine whether the cause(s) are systemic, repetitive or other causes that require timely remedial action.

    (b) Consider the continued relevance of the firm's quality objectives, whether all quality risks have been identified and appropriately assessed and whether the responses to quality risks remain appropriate. (Ref: Para. A95)

47. The firm shall implement remedial actions, as appropriate, that are responsive to the cause(s) of deficiencies and the related effect. (Ref: Para. A96)

Assessing the Effectiveness of the Monitoring and Remediation Process

48. The firm, including those assigned ultimate responsibility and accountability for quality, shall monitor the effectiveness of the remedial actions designed and implemented to address the cause(s) and evaluate whether the remedial actions appropriately address the deficiencies identified. (Ref: Para. A97)

Communicating Matters Related to Monitoring and Remediation

49. The firm shall communicate, on a timely basis or at least annually, relevant information about the results of the firm's monitoring and remediation to engagement teams, personnel performing functions in relation to the operation of the firm's system of quality management, including those who are ultimately responsible and accountable for quality, and parties that are external to the firm, as appropriate. Information communicated shall include the following: (Ref: Para. A40, A98–A99)

    (a) A description of the monitoring procedures performed.

    (b) Information about deficiencies, the causes of such deficiencies and remedial actions.

    (c) The conclusions drawn from monitoring and remediation.

Considerations Relating to Networks

50. [Placeholder – networks to be further considered] Some firms operate as part of a network and, for consistency, may implement some of their monitoring procedures on a network basis. Where firms within a network operate under common monitoring policies or procedures designed to comply with this ISQC, and these firms place reliance on such a monitoring system, the firm's policies or procedures shall require that:

    (a) At least annually, the network communicate the overall scope, extent and results of the monitoring process to appropriate individuals within the network firms; and

    (b) The network communicate promptly any identified deficiencies in the system of quality control to appropriate individuals within the relevant network firm or firms so that the necessary action can be taken,

    in order that engagement partners in the network firms can rely on the results of the monitoring process implemented within the network, unless the firms or the network advise otherwise.

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Application and Other Explanatory Material

The Firm's System of Quality Management (Ref: Para. 3–8)

A1. Governance principles form the framework for how the firm's decisions are made and therefore promote an environment that sustains and improves quality. Firm leadership has ultimate responsibility for quality and is accountable to the firm and the firm's stakeholders for the firm's quality. Nevertheless, firm leadership may assign responsibility for aspects of the firm's system of quality management to other individuals within the firm, which may include operational responsibility for the firm's system of quality management.

A2. Information and communication is the continual, iterative process of obtaining or generating and communicating information necessary to enable and support the proper functioning of the firm's system of quality management. Information and communication is necessary for all components of the firm's system of quality management, including governance and leadership and the firm's quality management process.

A3. The firm's quality management process encompasses the ongoing activities that support a risk-based approach to managing quality in the context of the overall objective in paragraph 16. These activities are interrelated and include the firm's monitoring of its system of quality management, which promotes the continual improvement of the firm's system of quality management. Such monitoring activities also include monitoring of the firm's governance and leadership and information and communication.

A4. Other pronouncements of the IAASB, for example ISA 220, ISRE 2400 (Revised)[5] and ISAE 3000 (Revised),[6] establish requirements for the engagement partner in relation to the management of quality at the engagement level that include managing risks to quality and implementing responses at an engagement level. Furthermore, ISA 220 establishes requirements for the engagement partner to consider whether there are other risks to quality and to identify responses to manage engagement quality.

Firm level (ISQC)	Required quality objectives, quality risks and responses established in ISQC 1 for the firm. Additional responses in ISQC 2.	Firm establishes quality objectives, identifies quality risks and designs and implements responses.
Engagement level (ISA 220)	Required quality risks and responses established in ISA 220 for the engagement partner.	Engagement partner considers whether there are other risks to quality and designs and implements responses to manage engagement quality.

Definitions

Reasonable Assurance (Ref: Para. 17(t))

A5. Reasonable assurance is a high level of assurance and is obtained when the firm's system of quality management is effective in reducing the risk that the firm does not achieve its overall quality objective, that is, the objective of this ISQC set forth in paragraph 16 to an acceptably low level. However, the firm is not required to obtain an absolute level of assurance, because there are inherent limitations of a firm's system of quality management. Such limitations include the reality that human judgment

[5] International Standard on Review Engagements (ISRE) 2400 (Revised), *Engagements to Review Historical Financial Statements*

[6] International Standard on Assurance Engagements (ISAE) 3000, *Assurance Engagements Other than Audits or Reviews of Historical Financial Information*

in decision-making can be faulty and that breakdowns in the firm's system of quality management may occur because of human error or behavior.

A6. When deficiencies are identified, this ISQC requires the firm to implement remedial actions to address the deficiencies identified, thereby providing the firm with reasonable assurance that it has achieved the overall objective in paragraph 16. Nevertheless, the identification of deficiencies within the firm's system of quality management may not necessarily indicate that the firm's system of quality management is not achieving its objective because the concept of reasonable assurance recognizes that some deviations in the firm's system of quality management may occur, for example:

- An identified deficiency may not be pervasive to all engagements (i.e., it is limited to a single engagement) and therefore may still provide the firm with reasonable assurance that the overall objective of its system of quality management has been achieved.
- Although a deficiency may have been identified in relation to a firm's response to a quality risk, the firm may have other responses that have been implemented to address the same quality risk for which no deficiencies have been identified.

Applying, and Complying with, Relevant Requirements (Ref: Para. 19)

A7. [To be updated to further enhance scalability] This ISQC does not call for compliance with requirements that are not relevant, for example, in the circumstances of a sole practitioner with no staff. Requirements in this ISQC such as those for policies or procedures for the assignment of appropriate personnel to the engagement team (see paragraph XX), for review responsibilities (see paragraph XX), and for the communication of the results of monitoring within the firm (see paragraph 49) are not relevant in the absence of staff.

Governance and Leadership, including Organization, Culture and Strategy (Ref: Para. 22–27)

A8. The governance principles in paragraph 22 are relevant to all firms and form the framework for how the firm's decisions take into account the overall objective of quality. In addition, law or regulation may prescribe how the firm is governed, for example, the firm may be required to follow an audit firm governance code that may incorporate more specific governance principles and require adherence to specific provisions. The firm may also establish governance principles that are more specific than the governance principles set out in paragraph 22. In establishing governance principles in relation to quality, the firm may take into consideration a variety of factors, including:

[Factors to be further developed by the Task Force, for example, in relation to external factors, the influence of the regulatory environment on the quality of certain of the firm's services, and in relation to internal factors, the size and diversity of services provided by the firm.]

A9. The firm's actions to implement the principles in relation to the governance of the firm may include establishing policies or procedures, assigning responsibility, communicating, providing training, or establishing resources. Paragraph 23 requires the firm to assign ultimate responsibility and accountability for quality to firm leadership and further requires firm leadership to take actions that address each of the principles in relation to the governance of the firm. Furthermore, paragraphs A12–A35 include examples of other actions the firm may implement to address such principles and through the quality management process, the firm may implement responses that also address the principles. For example, the firm's responses in relation to compliance with relevant ethical

requirements may assist the firm in embedding the firm's internal culture, in particular the professional and ethical values.

A10. The quality objectives, quality risks and responses to the quality risks that are established by the firm, as required by paragraphs 30–37, reflect the circumstances of the firm and therefore may change as a result of decisions made by the firm. For example, the firm's decision in relation to the organization of the firm or the allocation of resources may affect the identified and assessed quality risks or the responses that have been designed and implemented to address those quality risks. Accordingly, the results of decisions made by the firm, which are influenced by the firm's governance principles, may be a necessary and ongoing input into the firm's quality management process.

A11. In accordance with paragraph 39, the firm's monitoring activities include an evaluation of the implementation of the governance principles in relation to quality and whether the firm's leadership has assumed ultimate responsibility and accountability for quality. Paragraph 25 also establishes requirements in relation to periodic performance evaluations of individual(s) within the firm, which may form part of such monitoring activities.

Internal Culture (Ref: Para. 22(a), 23(a), and 23(b))

A12. Internal culture embodies the attitudes, values and behaviors exhibited by the firm and its personnel in its operations and interactions with its stakeholders. It is developed over time through beliefs, customs and rules. The firm's internal culture is an important factor in influencing how its personnel function in the interests of the public, while at the same time accomplishing the firm's commercial goals. A firm with a quality-focused culture recognizes and reinforces the importance of professional and ethical attitudes, values and behaviors and has a philosophy of accountability, transparency and continual improvement.

A13. Establishing an internal culture that fosters quality depends on clear, consistent, frequent and effective actions, including communication, at all levels within the firm that emphasize the firm's commitment to quality. The firm's chief executive officer (or equivalent) or the firm's managing board of partners (or equivalent), sets the tone at the top and the attitude to quality, including professional and ethical values, to support the firm's public interest role, through their operating style and personal conduct. This is further shaped and reinforced through the embracement by the firm's personnel of their role in embedding or demonstrating the desired professional and ethical behaviors that confirm the firm's commitment to quality. The actions undertaken by those assigned ultimate responsibility and accountability for quality to foster a culture of quality throughout the firm may include:

- Defining the purpose and ethical values of the firm, as well as the expected behaviors of the firm's personnel.
- Establishing trust through consistent, regular and open communication within the firm and through establishing policies or procedures to deal with complaints and allegations (i.e., whistleblowing).
- Establishing responsibility and accountability for quality, for example, through clearly defining and communicating roles and responsibilities throughout the firm and defining how internal quality will be measured.
- Providing transparency within the firm about the firm's actions to address quality, and the effectiveness of those actions.

- Establishing policies or procedures to address recruitment, development, compensation, and promotion with regard to its personnel that support and encourage behaviors that are consistent with the firm's purpose, values and strategy.
- Establishing appraisal and reward systems that promote personal characteristics that support and reinforce the firm's view on the importance of quality, and providing personnel with continuing professional development opportunities.
- Promoting a culture of consultation on difficult issues and providing access to high-quality technical support.
- Implementing robust systems for supporting decisions about the acceptance and continuance of client relationships and specific engagements.
- Monitoring the effectiveness of actions implemented to embed the culture and evaluating whether the outcome of monitoring activities are reflective of an internal culture that focuses on quality and the firm's public interest role.

The extent of such actions may depend on a variety of factors, including the size, structure, geographical dispersion and complexity of the firm. For example, a smaller firm may be able to influence the desired culture through less extensive actions due to the close interaction of firm leadership with the firm's personnel.

A14. Those assigned ultimate responsibility and accountability for quality also establish the firm's internal culture through the business strategy. A business strategy that aims to achieve an appropriate balance between long term sustainability and the need for the firm to achieve quality in all engagements recognizes that commercial considerations should not result in actions and decisions that impair quality. Commercial considerations that may impair quality may include excessive cost-cutting at times of economic downturn that damage the provision of quality in the medium term or internal training that is disproportionately focused on improving client service at the expense of necessary training to develop technical competence.

A15. The firm may carry out other actions to emphasize that each individual within the firm has a personal responsibility for quality and is expected to comply with the firm's policies or procedures.

Organization of the Firm (Ref: Para. 22(b) and 23(c))

A16. Organizing the firm in a manner that supports the effective design, implementation and operation of the firm's system of quality management may include:

- Establishing an internal firm structure that is commensurate with the size and operating characteristics of the firm and the services the firm provides;
- Designating authority and responsibility within the firm; and
- Maintaining and allocating sufficient and appropriate resources.

Internal Firm Structure

A17. The firm's internal structure comprises the leadership and management structure of the firm as well as how the firm is organized into divisions or geographical locations. The firm's leadership may be comprised of a managing board of partners or an independent governing body that has executive oversight of the firm, or committees may be established to fulfill specific leadership functions. At a

jurisdictional level, law or regulation may prescribe the structure or composition of firm leadership, for example, certain jurisdictions mandate the appointment of a governing body comprising a minimum number of independent non-executive members and prescribe the function or responsibilities of those appointed within these roles. Smaller firms may have simple structures comprising a single partner with responsibility for the oversight of the firm.

A18. In establishing the firm's leadership and management structure, the firm may take into consideration:

- The required knowledge, experience and capacity necessary to fulfill the identified roles; and
- The need for other attributes that contribute to improved quality, for example, appointing individual(s) who are independent or not involved in the operational aspects of the firm and are able to provide impartial judgment that enhances the firm's recognition of its public interest role and its commitment to quality.

Responsibility, Accountability and Authority (Ref: Para. 22(c) and 23)

A19. Firm leadership is allocated ultimate responsibility for quality and is accountable to the firm and the firm's stakeholders for the firm's quality. In circumstances when the firm appoints a managing board of partners (or equivalent), the managing board of partners (or equivalent) has responsibility for overseeing the firm's operations and therefore has a shared responsibility and accountability for quality.

A20. Accountability for quality may be established through various actions, including evaluating whether the quality management system achieves its overall objective. Communication of relevant information about the results of the firm's monitoring and remediation to those assigned ultimate responsibility and accountability for quality, as required by paragraph 49, supports the accountability of firm leadership for quality, since firm leadership has the responsibility to take prompt and appropriate action, where necessary, in response to such information. Paragraph 48 also requires those assigned ultimate responsibility and accountability for quality to monitor the effectiveness of the remedial actions designed and implemented to address the cause(s) of deficiencies and to evaluate whether the remedial actions appropriately address the deficiencies identified. The remedial actions to address causes(s) of deficiencies may relate to the design, implementation or operation of the firm's system of quality management, including the continued relevance of the firm's quality objectives, whether all quality risks have been identified and appropriately assessed and whether the responses to the risks remain appropriate.

Assigning operational responsibility for the firm's system of quality management (Ref: Para. 22(b), 23(c), and 24)

A21. Assigning operational responsibility for the firm's system of quality management establishes the authority of the person(s) to whom responsibility is assigned and facilitates decision-making within appropriate boundaries. Clearly communicating reporting lines, roles, authority and responsibilities to the firm's personnel supports those assigned such responsibility in performing their functions. Depending on the geographical dispersion, size, structure and complexity of the firm, the firm may determine it more effective to centralize responsibility for certain functions to achieve a desired level of consistency. However, in other cases the firm may determine that decentralizing such responsibilities is more effective.

A22. Sufficient and appropriate experience and knowledge enables the person(s) assigned operational responsibility for the firm's system of quality management to identify and understand quality management issues and to establish quality objectives, identify and assess quality risks and design and implement appropriate responses. Furthermore, it is necessary that the person(s) have sufficient time to adequately discharge their responsibilities.

A23. The accountability of those assigned operational responsibility for the firm's system of quality management is established through periodic performance evaluations that assess their effectiveness, as required by paragraph 25, and may be further established by:

- Clearly communicating roles, authority and responsibilities within the firm in order that personnel understand their function and the firm's expectations.
- Providing incentives for actions to be implemented through monitoring the firm's system of quality management, including:
    - Pre-defining internal quality measures, and evaluating such measures against targets.
    - Evaluating the effectiveness of the firm's process for establishing quality objectives and identifying and assessing quality risks.
    - Evaluating whether the firm's responses to the quality risks appropriately address the quality risks.
- Establishing appraisal and reward systems that address the responsibilities and promote personal characteristics that support and reinforce the firm's view on the importance of quality.

Resources (Ref: Para. 23(d))

A24. Establishing the necessary resources and allocating these appropriately is essential for the proper functioning of the firm's system of quality management and supporting the performance of the firm's engagements. Resources include:

- Financial resources that are available to the firm.
- Human resources who have appropriate competence and capabilities.
- Technology resources, for example, application systems and hardware.
- Intellectual resources, for example, the firm's development of a methodology or guides.

A25. Those assigned ultimate responsibility and accountability for quality are in a unique position to influence the extent of resources that the firm obtains and maintains, and how the firm's resources are allocated. Paragraph XX includes additional requirements regarding the firm's quality objectives, quality risks and responses addressing resources [Placeholder to link to the resources element in the quality management process section once this is further developed].

Stakeholder Confidence (Ref: Para. 22(d) and 23(e))

A26. The firm may have a variety of stakeholders, including the network or other network firms, audit oversight bodies and other external bodies, those charged with governance of the firm's clients or users of the firm's reports. In enhancing stakeholder confidence in the public interest aspects of the firm's decision making, the firm takes into account the legitimate and reasonable needs, interests and expectations of all stakeholders in formulating decisions, i.e., in addition to considering what is in the

best interests of the firm, the firm also gives consideration to its stakeholders. This supports the firm's recognition of its public interest role.

A27. Stakeholders' perception of the quality of engagements performed by the firm may be improved when they consider that the firm supports and embeds a quality-focused culture that emphasizes the firm's public interest role. Confidence may be increased if stakeholders are made aware of the firm's activities that it has undertaken to address quality, and the effectiveness of those actions. As a result, the firm's ability to maintain stakeholder confidence in the quality of its engagements may be enhanced through effective two-way communication between the firm and its stakeholders. How the firm effects such communication may vary, for example the firm may assign responsibility for stakeholder communication to a governing body who are able to independently initiate dialogue with the firm's stakeholders and prompt feedback in a manner that facilitates candid discussion. In some circumstances, the firm may communicate with stakeholders through a transparency report. Paragraph XX addresses circumstances when the firm is required to prepare a transparency report, [Placeholder for when transparency reporting is further developed].

Performance Evaluations (Ref: Para. 25)

A28. Firm leadership's accountability for quality is also established by evaluating the effectiveness of firm leadership overall, as well as the performance of individuals within firm leadership. Paragraph 25 requires the firm to establish ongoing performance evaluations that assess the effectiveness of the person(s) that are assigned ultimate responsibility and accountability for quality. Given the unique position of firm leadership, such evaluations may be undertaken by an independent non-executive member of the firm's governing body, a special committee, or an external service provider.

A29. Undertaking periodic performance evaluations of individual(s) within the firm supports the firm's evaluation of whether the governance principles in relation to quality have been implemented through appropriate actions and whether the firm's leadership has assumed ultimate responsibility and accountability for quality, as required by paragraph 39.

[Placeholder for additional application material related to performance evaluations that may include:

- Specific consideration of the firm's monitoring results and the effective operation of the quality management process.
- Measuring performance against the leadership responsibilities in paragraph 23.]

Whistleblowing (Ref: Para. 26–27)

A30. Establishing policies or procedures to deal with whistleblowing (i.e., complaints and allegations) supports the firm's internal culture of fostering quality and ethical values. The firm's process to enable reporting of complaints and allegations may include establishing clearly defined channels for firm personnel to raise any concerns in a manner that enables them to come forward without fear of reprisals.

A31. Complaints and allegations (which do not include those that are clearly frivolous) may originate from within or outside the firm and may relate to the failure of the work performed by the firm to comply with professional standards and applicable legal and regulatory requirements, or non-compliance with the firm's system of quality management. Complaints and allegations could be made by engagement team members, other firm personnel, clients or other third parties.

A32. Policies or procedures established for the investigation of complaints and allegations may include, for example, that the person(s) supervising the investigation:

- Has sufficient and appropriate experience;
- Has authority within the firm; and
- Is otherwise not involved in the engagement or has sufficient objectivity from the area or personnel of the firm subject to the investigation.

The person(s) supervising the investigation may involve legal counsel as necessary. In the case of a small firm, it may not be practicable for the partner supervising the investigation not to be involved in the engagement or other subject matter of the investigation. As a result, such firms may use the services of a suitably qualified external person or another firm to carry out the investigation into complaints and allegations.

A33. In investigating complaints and allegations, the firm may have a responsibility to determine whether law, regulation or relevant ethical requirements impose an obligation on the firm to report the matter to an authority outside the firm.

A34. Paragraphs 44–48 explain the actions that may be taken by the firm to address deficiencies in the design, implementation or operation of the firm's system of quality management. Such actions include consideration of the continued relevance of the firm's quality objectives, whether all quality risks have been identified and appropriately assessed and whether the responses to quality risks remain appropriate. Furthermore, the firm may monitor the effectiveness of the remedial actions designed and implemented to address the causes of deficiencies.

A35. If the firm operates as part of a network, there may be circumstances when the firm may determine it appropriate to report a complaint or allegation in relation to another network firm, for example, the firm may identify an error in the methodology developed by the network firm. In such circumstances, the remedial actions taken by the firm may include determining whether the network firm has taken appropriate remedial action and monitoring the effectiveness of such actions.

Information, Communication and Documentation

Information and Communication (Ref: Para. 28 and 49)

A36. Obtaining or generating and communicating information is an ongoing process that involves all firm personnel and encompasses the dissemination of information within the firm and externally. Information that is relevant, accurate, complete, timely and valid is necessary for the proper functioning of the firm's system of quality management, and may be obtained from both internal and external sources.

A37. Communication is the means through which the firm and its personnel share relevant information to support the proper functioning of the firm's system of quality management. Paragraph 28 identifies the parties with whom communication is required, which may include communication among those parties. For example, personnel performing functions in relation to the operation of the firm's system of quality management may obtain information in relation to external inspection findings from an external oversight authority and may communicate relevant aspects of this information to engagement teams.

A38. Information relating to the firm's system of quality management that the firm communicates to the firm's engagement teams may include the following:

- Information related to the firm's culture, for example, the message that each individual has a personal responsibility for quality and is expected to comply with the firm's policies or procedures.
- The firm's responses to quality risks, for example, policies or procedures in relation to the firm's system of quality management that engagement teams are expected to apply at an engagement level (e.g., the firm's policies or procedures in relation to acceptance and continuance of engagements).
- Information that describes the authority, roles and responsibilities of personnel performing functions in relation to the engagement.
- Information related to monitoring and remediation, for example, relevant information about the results of the firm's monitoring and remediation, as contemplated by paragraph 49 of this standard.
- [Placeholder - add an additional example on communicating inspection findings on component auditors once networks has been further developed]

A39. Information relating to the firm's system of quality management that is relevant to personnel performing functions in relation to the operation of the firm's system of quality management, including those who are ultimately responsible and accountable for quality, may include the following:

- Information that describes the authority, roles and responsibilities of personnel performing functions in relation to the operation of the firm's system of quality management.
- Information that supports the oversight of the firm's system of quality management by those who are ultimately responsible and accountable for quality, for example, changes in the firm and its environment, applicable law, regulation or relevant ethical requirements, and the results of the firm's monitoring and remediation, as contemplated by paragraph 49 of this standard.
- Information relevant to establishing the quality objectives, identifying and assessing the quality risks and designing responses, for example, the types of services the firm provides, the industries it serves and the entities to whom services are provided or, when the firm operates as part of a network, the extent to which the network has addressed the quality objectives, quality risks and related responses [Placeholder for networks – may need to be revisited once networks has been further considered].
- Information relevant to the operation of the responses identified, including information obtained from engagement teams, for example, information regarding the financial interests of the firm's personnel that enables the firm to identify and evaluate threats to the firm's independence, information communicated by an engagement team regarding non-audit services provided to an entity or information communicated by engagement quality control reviewers.
- Information related to monitoring and remediation, for example, relevant information about the results of the firm's monitoring and remediation, as contemplated by paragraph 49 of this standard.

A40. Communication with those who are ultimately responsible and accountable for quality provides them with the information needed to exercise their oversight of the firm's system of quality management,

including monitoring the effectiveness as well as the appropriateness of remedial actions in response to identified deficiencies, as contemplated by paragraph 48 of this standard.

A41. Parties that are external to the firm may include the network, network firms, external oversight authorities, users of the firm's reports or the firm's clients, external service organizations or the firm's legal counsel. Information that is exchanged with parties that are external to the firm may include the following:

- Information about the firm or network's monitoring activities between the firm and the network. [Placeholder to refer to interaction with networks]
- Information relating to the design, development and performance of the firm's system of quality management communicated to external oversight authorities.
- Information relating to external inspection findings that is received by the firm from external oversight authorities.
- Information about the firm's internal indicators of audit quality that is communicated to the firm's stakeholders (e.g., through the firm's transparency report).
- Information relating to the firm's compliance with the requirements of professional standards and applicable legal and regulatory requirements, for example, information required by professional bodies with respect to the registration of the firm's engagement partners.
- Communication to external service organizations relating to the firm's policies or procedures.

A42. [Placeholder for reference to the requirements in ISA 220 addressing communication with the firm and also to consider examples of communication with personnel outside the firm, e.g., shared service centers. Examples include:

- Information on identified threats or breaches of the firm's independence policies or procedures.
- Information in respect of the engagement strategy that is relevant to the firm's monitoring activities.
- Information in relation to the firm's policies or procedures in respect of new engagements.]

A43. Establishing policies or procedures to facilitate communication of relevant information supports a proper functioning of the firm's system of quality management. Such policies or procedures may include specifying the nature of the information, the individuals within the firm with whom such information should be communicated and the frequency and manner of the communication. Paragraph 26 also requires the firm to establish policies or procedures addressing whistleblowing, which may include establishing processes for the communication of matters on an anonymous or confidential basis.

A44. There are a variety of methods the firm may use to communicate information, for example, manuals of policies or procedures, newsletters, alerts, systems (e.g., the firm's engagement software), emails, intranet or other web-based applications, training, presentations, social media, webcasts or through one-on-one discussions. In determining the most appropriate method(s) and frequency of communication, the firm may take into consideration the nature and urgency of the information being communicated and the audience to whom the information is being communicated. In some circumstances, the firm may determine it necessary to communicate the same information through multiple methods in order to achieve the objective of the communication and in such cases the

consistency of the information communicated is important to its effectiveness. In considering the method of the communication, the firm may take into consideration cultural, ethnic and generational differences in order to enable effective communication (e.g., the firm may translate information into different languages).

A45. In accordance with paragraph 39(b), the firm's monitoring activities include an evaluation of the firm's information and communication and whether it enables and supports the proper functioning of the firm's system of quality management.

Considerations Specific to Smaller Firms

A46. Communication internally within a smaller firm is likely to be undertaken in a more direct manner as there are fewer personnel with whom to communicate. In such circumstances, communication processes and methods may be less structured. The external parties with whom the firm communicates may also be less extensive in a smaller firm. For example, the smaller firm may not belong to a network, may not be subject to oversight by external authorities or may not perform engagements in relation to entities that have a public interest and therefore has a fewer number of users of the firm's reports.

Quality Management Process (Ref: Para. 30–50)

A47. The firm's process for establishing the quality objectives, identifying and assessing the quality risks, and designing and implementing responses involves the consideration of both internal and external factors. Examples of internal and external factors include:

- Economic, regulatory, jurisdictional, technological and social factors.
- The organization of the firm, including the geographic dispersion, use of audit delivery models, shared service centers or outsourced service providers.
- The firm's resources, including technology, intellectual and human resources.
- The types of services the firm provides, the industries it serves and the nature of the entities to whom the services are provided.
- The firm's stakeholders, for example, users of the firm's reports, regulatory authorities, preparers and those charged with governance.

Establish Quality Objectives (Ref: Para. 30–32)

A48. The firm establishes quality objectives specific to the firm's circumstances, based on the quality objectives set out in paragraph 32 that support the overall objective of this ISQC set out in paragraph 16 (the overall objective of the system of quality management). The firm may also establish additional objectives in relation to other aspects of the firm that are not relevant to the overall objective of the firm's system of quality management, for example, objectives in relation to its financial performance or future growth.

A49. Quality objectives are established at an appropriate level of granularity that allows for the quality risks to be appropriately identified, assessed and addressed. Larger and more complex firms may establish quality objectives at a firm level, and cascade more granular quality objectives to various levels within the firm. On the other hand, smaller and less complex firms may cascade more granular

quality objectives directly to the engagement level, for example, in circumstances where the firm performs a limited number of engagements to which the quality objective relates.

A50. In establishing the quality objectives, the firm also considers the firm's governance principles in relation to quality and whether such objectives support and are consistent with such principles. Furthermore, given that the firm's quality objectives reflect the circumstances of the firm, they are affected by the decisions of the firm that are guided by the firm's governance principles. In some circumstances, the firm may establish specific quality objectives that relate directly to the governance principles in relation to quality.

A51. Quality objectives may be established to apply to the entire firm or may be categorized by engagements performed by the firm or the firm's personnel. For example, the firm's quality objectives related to independence may be established to apply to the entire firm or all firm personnel, whereas the firm's quality objectives related to compliance with professional standards may be categorized to apply to the services performed by the firm or the personnel performing those services.

A52. In establishing the quality objectives, paragraph 31(b) requires the firm to consider whether the quality objectives are relevant to the circumstances of the firm and whether all relevant quality objectives have been identified. In addition, the firm may also consider the continued relevance of the quality objectives as a result of, for example:

- Changes in the factors and circumstances affecting the firm (e.g., a new service offering, changes in the firm's environment or other factors set out in paragraph A47).
- Other information, such as the results of monitoring activities or information communicated by engagement teams related to the firm's system of quality management.

Accordingly, the frequency of the firm's consideration of the continued relevance of the quality objectives, including whether all relevant quality objectives have been identified depends on the rate of change in the factors and circumstances affecting the firm, the timing of when other information becomes available to the firm and the urgency of responding to such changes or information in the context of the firm's system of quality management.

A53. When establishing the quality objectives for the first time, the firm may establish the quality objectives based on the firm's existing system of quality management (i.e., taking into consideration the activities that are already established by the firm and determining the intended purpose of such activities). The firm may also establish additional quality objectives, or may determine that the activities do not relate to quality objectives that are relevant to the overall purpose of the firm's system of quality management.

Perform Quality Risk Assessment (Ref: Para. 33–34)

A54. The identification and assessment of the quality risks forms the basis for the firm's determination of the nature, timing and extent of the firm's response to such quality risks and influences how the firm allocates its resources. In the process of identifying the quality risks, the firm may also identify additional quality objectives that have not already been established.

A55. The firm's process for identifying and assessing the quality risks may involve a combination of ongoing and periodic risk identification and assessment procedures. The firm identifies the quality risks that, individually or in combination, could reasonably have an adverse impact on the firm's ability

to achieve the overall objective, i.e., the firm is not required to identify risks to quality that the firm believes may have a limited effect on the firm's ability to achieve its overall objective.

A56. The nature of the quality risks that are identified and the assessment of their likelihood and impact varies based on the firm and its circumstances, and includes the internal and external factors set out in paragraph A47. For example:

- Firms that perform more complex engagements may have a heightened need for technical resources to support consultation and accordingly the risk that such resources are not available may be more significant for such firms.
- The impact of the loss of an engagement partner on a smaller firm may be more significant than for a larger firm and accordingly the quality risk in relation to the loss of engagement partners may be assessed to have a greater impact for such firms.

A57. Similar to the considerations in relation to quality objectives, the firm may consider the continued relevance of the quality risks, including whether all relevant quality risks have been identified as a result of, for example:

- New or changes to the conditions, events, circumstances, actions or inactions that could affect the firm's ability to achieve its quality objectives.
- Other information, such as the results of monitoring activities, including external inspections, or information communicated by engagement teams related to the firm's system of quality management.

Accordingly, the frequency of the firm's quality risk identification and assessment depends on the rate of change of the above factors, the timing of when other information becomes available to the firm and the urgency of responding to such changes or information in the context of the firm's system of quality management.

A58. When identifying the quality risks for the first time, the firm may identify the quality risks based on the firm's existing system of quality management, i.e., taking into consideration the activities that are already established by the firm and determining the quality risks that such activities are intended to address.

A59. In assessing the likelihood and impact of the quality risks, the firm may take the following factors into consideration:

- The likelihood of whether or not the quality risk could occur and the expected frequency of its occurrence.
- The rate at which the impact would take place, or the amount of time that the firm has to respond to the quality risk. For example, when changes in professional standards are effected, there is typically a period of time allowed for implementation. On the other hand, the effect of high turnover of firm personnel may be more immediate and the firm may not have been able to prepare for such an event.
- The duration of time of the impact after the quality risk has occurred. For example, a change in a professional standard may have a more long-term impact when it becomes effective, since the firm may need to train its personnel on the changes or update methodology, although the effect of such change may lessen over time. Conversely, a breach of the firm's independence policies or procedures may have a more short-term or immediate effect.

Design and Implement Responses to Quality Risks (Ref: Para. 36–37)

A60. A response to a quality risk comprises the firm's actions to address a quality risk. Such actions may include, among others, establishing policies or procedures, assigning responsibility, communicating, providing training, performing reviews or establishing resources. In some circumstances, the firm may determine that the quality risk is so significant that it is best avoided, for example, the firm may determine that a particular service will not be offered, or the firm will not provide services to a particular industry or type of entity.

A61. Paragraph 22 requires the firm to implement governance principles in relation to quality. In addition to addressing the quality risks, the firm's responses may also address the firm's governance principles. For example, the firm's responses in relation to compliance with relevant ethical requirements may assist the firm in embedding the firm's internal culture, in particular the professional and ethical values.

Policies or Procedures

A62. Policies or procedures reflect the internal culture of the firm and clearly establish what is expected, and who is responsible and accountable. Structured documentation of the firm's policies or procedures may not be necessary in all circumstances, for example, the policies or procedures could be stated in communications or implied through the actions and decisions of firm leadership. The extent to which the firm establishes policies or procedures, and the manner in which those are documented and communicated, depends on the circumstances of the firm. Nevertheless, a lack of awareness of the firm's policies or procedures and the circumvention of policies or procedures is more possible when they are not documented. In a more complex firm, establishing robust policies or procedures that are well documented may be more important in order to achieve consistency across the firm.

A63. Throughout this ISQC, the firm is required to establish policies or procedures in relation to specific areas of the system of quality management, for example, the prescribed responses in paragraph 37 [see also **Agenda Item 2–C**] require the firm to establish policies or procedures in order to address the quality risks set out in this standard. However, the responses designed and implemented by the firm to address quality risks that are additional to the prescribed responses in paragraph 37 may comprise forms of responses other than policies or procedures, for example, those explained in paragraph A60.

Nature, Timing and Extent of the Firm's Response

A64. The assessment of the quality risk affects the firm's responses, for example, certain quality risks may not require any action to reduce the likelihood or impact further or the firm may choose to avoid the risk. In other circumstances, due to the assessment of the quality risks, additional or more rigorous responses may be required.

A65. The nature, timing and extent of the firm's responses to the identified quality risk depends on the conditions, events, circumstances, actions or inactions that give rise to the quality risk. For example, if the firm's quality risk relates specifically to a particular industry or category of clients (e.g., audits of financial statements of listed entities), the firm's responses may only require specific actions in

relation to clients in the industry or that are within the category, rather than all engagements performed by the firm.

A66. The nature, timing and extent of the firm's responses may also vary based on factors such as the size and complexity of the firm. For example, in a smaller firm, due the concentration of the firm's operations, the closer oversight by the firm's leadership may be an effective and appropriate response to certain risks. In addition, in some circumstances, the response may be most effectively established at an engagement level, for example, a smaller firm may perform only a few engagements of a specific type and it may be more effective for the quality risk to be addressed directly at the engagement level rather than establishing formal policies or procedures at the firm level that are cascaded down to an engagement level.

A67. In designing a response to a quality risk, the firm may take many factors into consideration, including:

- Whether the response should involve a preventative activity that would avoid the conditions, events, circumstances, actions or inactions, or whether an activity that is more detective in nature would be appropriate. For example, developing the competence and capabilities of engagement team members through training, supervision and review assists in the prevention of conditions, events, circumstances, actions or inactions, whereas a pre-issuance review at the end of the engagement is more detective in nature.
- Whether the response should be a manual process or whether the quality risk would be more appropriately addressed through automated means, for example, the firm may be able to use data analytic techniques or other technologies.
- The appropriate timing of the response activities, for example, certain activities may need to operate on a continuous basis in order to be effective (e.g., monitoring and reporting breaches of the firm's independence policies or procedures).
- Whether the response alone is sufficient to address the quality risk, i.e., a combination of responses may be necessary to appropriately address the quality risk.
- Whether there are responses that address multiple quality risks and therefore may be more effective to design and implement.
- The appropriate resources to support the response. For example, certain responses may need to be performed by competent personnel with the appropriate knowledge, time and experience, or the firm may need to source technological or intellectual resources to support the functioning of the response (e.g., application systems and hardware or a firm methodology for the performance of engagements).
- The information to be obtained, generated and communicated in relation to the response.

A68. In addition to these factors, as part of designing the firm's response the firm may address how deviations should be addressed. For example, in relation to a pre-issuance review, the firm may indicate how engagement deficiencies should be addressed, or in relation to training firm personnel, the firm may specify the repercussions on firm personnel who do not attend the training.

A69. Certain responses may be designed as in-process monitoring activities and are unrelated to the firm's monitoring and remediation process. For example, the firm may implement activities to monitor breaches of the firm's independence policies or procedures and as part of the firm's monitoring and

remediation process, the firm may monitor the in-process independence monitoring activities to determine whether they effectively address the quality risks related to independence.

A70. Similar to the considerations in relation to the quality objectives and quality risks, the firm may consider the continued appropriateness of the responses, including whether other responses may be more effective. For example, new software may be introduced that allows the firm to more effectively address a particular risk, or the firm may reallocate responsibilities. Furthermore, the results of monitoring activities, including external inspections, or information communicated by engagement teams related to the firm's system of quality management may also indicate the need for the responses to be considered. Accordingly, the frequency of the firm's consideration of the continued appropriateness of the responses and whether other responses may be more effective depends on changes in the firm's quality objectives and quality risks, as well as when information becomes available to the firm and the urgency of responding to such information.

Monitoring and Remediation

Establishing a Monitoring and Remediation Process (Ref: Para. 38)

A71. In addition to supporting the firm's evaluation of whether the system of quality management provides the firm with reasonable assurance that its overall objective has been achieved, monitoring and remediation facilitates the improvement of engagement quality and the firm's system of quality management.

A72. A monitoring and remediation process typically involves the following steps:

- Design monitoring activities, including the nature, scope and frequency of such activities;
- Perform internal monitoring activities;
- Assess the results of the monitoring activities and external inspections, in order to identify deficiencies in the firm's system of quality management;
- Address deficiencies identified if there is an indication that a report may be inappropriate or that procedures were omitted during the performance of an engagement
- Determine the cause(s) of deficiencies and evaluate the effect of deficiencies;
- Implement appropriate remedial action(s);
- Monitor the effectiveness of the remedial actions and evaluate whether the remedial actions appropriately address deficiencies; and
- Communicate matters in relation to monitoring and remediation.

Monitoring the Firm's System of Quality Management (Ref: Para. 39–40)

A73. Monitoring of the implementation of the governance principles in relation to quality includes evaluating the actions of leadership with respect to the organization, culture and strategy of the firm.

A74. In determining the scope and frequency of the monitoring activities, in addition to the matters set out in paragraph 40, the firm may consider other factors such as:

- The size of the firm, the types of services the firm provides, the industries it serves and the nature of the entities to whom services are provided.

- The structure and organization of the firm, including the involvement of the network firm in monitoring activities.
- The firm's infrastructure, for example, technology and resources to support monitoring activities.
- The firm's assessment of the quality risks identified (e.g., the firm may determine that ongoing monitoring activities are necessary in relation to responses that address higher quality risks).

A75. The frequency of the firm's monitoring activities may comprise ongoing monitoring activities that are embedded within the firm's quality management process, periodic monitoring activities or a combination of both. Ongoing monitoring activities are generally described as routine activities, built into the firm's processes and performed on a real-time basis, reacting to changing conditions, for example, computerized continuous monitoring techniques over engagement file retention procedures. Periodic monitoring activities are conducted at certain intervals by the firm, for example, inspection of engagements. Since periodic monitoring activities are performed at certain intervals, ongoing monitoring activities may be more effective in identifying deficiencies in the system of quality management in a timely manner. Nevertheless, periodic monitoring activities may be useful in confirming the results of ongoing monitoring activities.

A76. The nature, scope and frequency of the firm's monitoring activities need to be sufficient for the firm to establish whether its system of quality management is effective, and remains effective, in providing it with reasonable assurance that its overall objective has been achieved, or whether changes in the firm's system of quality management should be made. For example:

- The firm's monitoring activities in relation to evaluating whether the business strategy reflects the professional and ethical values of the firm and recognizes the need for the firm to achieve quality in all engagements of the firm may be performed periodically. If there have been no changes in the firm's business strategy, the firm's monitoring activities may not need to be performed frequently.
- The firm may determine that more frequent monitoring activities are needed in relation to certain types of engagements, for example, entities operating in industries that are subject to frequent change or engagements where a high number of deficiencies have been identified through previous monitoring activities. Such monitoring activities may be ongoing, for example, a pre-issuance review, or may be performed periodically such as an annual inspection of an engagement.
- Due to the increased risk of deficiencies, the firm's monitoring activities in relation to matters related to independence may comprise ongoing activities in order that breaches of independence are identified in a timely manner, and may include automated systems to capture and monitor information. The firm may also perform periodic monitoring activities, such as inspecting personnel's financial affairs for compliance with the firm's independence policies or procedures.

A77. Examples of monitoring activities may include:

- Evaluating actions by leadership in establishing an appropriate tone at the top and culture that supports quality.
- Interviewing firm personnel to evaluate the effectiveness of the firm's communication in relation to certain matters.

- Evaluating who within the firm has been assigned responsibility for establishing the quality objectives, identifying and assessing quality risks and designing responses to the quality risks, and how such personnel have gone about doing so.
- Peer reviews, or other types of reviews, designed with the purpose of monitoring areas of the firm's system of quality management.
- Automated alerts in relation to engagements, for example, automatic notifications when policies are not applied.
- Inspecting records regarding the provision of non-audit services by other service lines within the firm to establish that prohibited services were not provided to an audit client.
- Checking records of attendance at training events for compliance with the firm's policies on professional development.
- Inspecting time records for (i) number of hours spent by engagement partners and other senior personnel and assessing the appropriateness of such hours; or (ii) evidence of involvement of experts on certain types of engagements such as audits performed in respect of certain industries, to determine the appropriate use of experts.

A78. The purpose of monitoring activities is evaluate the design, implementation and operation of the firm's system of quality management, including the responses designed and implemented by the firm in response to quality risks. In some circumstances, the firm may implement procedures in response to quality risks that, by their nature, may appear to fulfill the purpose of monitoring activities. For example, the firm may implement procedures to monitor breaches of the firm's independence policies or procedures as a response to a particular quality risk in relation to the firm's compliance with relevant ethical requirements. Although such procedures may be described as monitoring activities, they form part of the firm's responses to quality risks, and as such are subject to the firm's monitoring process.

A79. The firm's system of quality management may change as a result of various factors, for example:

- Changes in factors that affect the quality objectives and quality risks (e.g., a new service offered by the firm or changes in the firm's environment).
- Changes to address an identified deficiency in the firm's system of quality management.
- Other factors, such as the firm amends the responses to quality risks because these become obsolete over time or more effective responses are designed and implemented

When changes occur, previous monitoring activities undertaken by the firm may no longer provide the firm with information to support the evaluation of its system of quality management and therefore the firm's monitoring activities may include monitoring areas of change. Furthermore, previous monitoring activities undertaken by the firm may also no longer provide the firm with information to support the evaluation of its system of quality management in relation to areas that have remained the same, for example, because of the time period since the monitoring activities were undertaken. Accordingly, the firm considers the continuing relevance of previous monitoring activities, which includes understanding changes in factors that impact the firm's system of quality management, as well as when such monitoring activities were performed.

A80. The outcome of the firm's previous monitoring activities may also indicate areas where monitoring activities should be undertaken, for example, monitoring may need to be undertaken in certain areas

where there is a history of deficiencies. The firm may also obtain other information that may suggest deficiencies in the firm's system of quality management and therefore may indicate the need for the firm to conduct monitoring activities, for example, the firm may conduct monitoring activities in response to the results of external inspection findings in order to further understand such findings and their effect on the firm.

Engagement inspections (Ref: Para. 41)

A81. Paragraph 41 requires an inspection of at least one completed engagement for each engagement partner, on a cyclical basis determined by the firm, which is ordinarily three years. In addition, the firm establishes criteria to determine other engagements for inspection that, together with the engagements subject to cyclical inspection, provide a sufficient basis to enable the firm to evaluate its system of quality management. Such criteria may include:

- Engagements where the firm or engagement partner are inexperienced, for example, a new industry, service offering or new engagement partner.
- The inspection of particular engagements on a more regular basis, for example, engagements performed in respect of certain entities (e.g., a listed entity).
- Engagements subject to external inspection that have negative findings, or engagements where the results of previous internal inspections identified deficiencies.
- Engagements where there has been a material restatement of comparative information in the financial statements or the firm's report required reissuance.

A82. The nature, timing and extent of the inspection cycle and the frequency of selection of individual engagement partners or individual engagements, depends on many factors, such as the following:

- The size of the firm, including the number and geographic location of offices.
- The nature and complexity of the firm's practice and organization.
- Who performs the inspection, for example, whether it is the individual office, the firm or the network firm.
- The extent of other monitoring procedures implemented by the firm, for example, peer reviews undertaken in conjunction with other firms or certain types of pre-issuance reviews that qualify as monitoring activities.

A83. Evaluating completed engagements involves performing procedures designed to provide evidence of compliance by engagement teams with the aspects of the firm's system of quality management relevant to the engagement. In determining the nature and extent of the procedures to be undertaken in performing the evaluation of completed engagements, the firm may take into consideration a variety of factors, for example, the assessment of quality risks or areas of change in the firm's system of quality management (e.g., circumstances when the firm has introduced a new policy or procedure). Such procedures may also include performing substantive reviews of the quality of work performed, in particular significant judgments made by the engagement team and the related conclusions reached in forming the overall conclusion on the engagement and in preparing the engagement report.

Objectivity of those performing monitoring activities (Ref: Para. 42)

A84. The determination of whether those performing monitoring activities are sufficiently objective depends on the activity subject to monitoring. For example, an activity involving the exercise of judgment may necessitate heightened objectivity by those performing the monitoring activities than activities with no judgment (e.g., the monitoring of the firm's policies or procedures addressing differences of opinion). In some circumstances, the monitoring activities in relation to an activity that is automated could be undertaken by those involved with the activity (e.g., the monitoring of the firm's automated process for identifying breaches of the firm's independence policies or procedures). In considering the objectivity of those performing the monitoring activities, the firm may take into consideration the relevant ethical requirements that may explain factors or circumstances that create a threat to objectivity.

A85. Factors or circumstances that may create a threat to objectivity in the case of a monitoring activity involving the inspection of an engagement may include the following:

- A self-review or familiarity threat may arise when the person performing the engagement inspection is a member of the engagement team, the engagement quality control reviewer or was consulted on matters related to the engagement.
- A familiarity threat may arise when the person performing the engagement inspection is a close or immediate family member of the engagement partner, engagement quality control reviewer or another key member of the engagement team.
- An intimidation threat may arise in circumstances when the engagement partner is an aggressive or dominating individual, or the person performing the inspection is in the chain of command of the engagement partner.

Identifying and Remediating Identified Deficiencies

Evaluating the results of the monitoring activities (Ref: Para. 43)

A86. Deficiencies in the firm's system of quality management include matters that have the potential to adversely affect the firm's ability to achieve its overall objective. The firm may also identify opportunities to improve the firm's system of quality management as a result of the evaluation of the results of the monitoring activities and external inspections.

A87. The timing of when the firm evaluates the results of the monitoring activities and external inspections may vary. For example, the firm may obtain and evaluate results from ongoing monitoring activities and external inspections on a real-time basis and evaluate such results in real time, thereby enabling the firm to identify the deficiencies and implement remedial actions on a timely basis. However, in other circumstances the firm may evaluate the results of the monitoring activities and external inspections periodically.

A88. A deficiency in the firm's system of quality management may also be identified from sources other than monitoring activities, for example, information from the firm's activities in response to quality risks (e.g., the activities explained in paragraph A78) or information from its whistleblowing program.

Determining the cause of deficiencies (Ref: Para. 45–46)

A89. The objective of determining the cause(s) of deficiencies is to understand the underlying circumstances that caused the deficiencies. An improved understanding of the underlying cause(s) of deficiencies:

- Facilitates the implementation of more effective actions to address deficiencies, thereby improving quality.
- Directly contributes to the improvement of quality at the engagement level through the participation of engagement teams in the causal analysis process.
- Enables those assigned ultimate responsibility and accountability for quality to have an improved awareness, to enable them to proactively monitor actions taken to address deficiencies.
- Facilitates more effective communication to firm personnel by explaining the actual cause(s) of deficiencies, rather than the deficiencies themselves.

A90. The nature, timing and extent of the procedures undertaken by the firm to determine the cause(s) of deficiencies are affected by the nature of the deficiencies identified, and may include the following factors:

- In circumstances when a deficiency relates to an engagement, whether it appears unique to the individual engagement or appears more systemic and repetitive across many engagements.
- In circumstances when a deficiency relates to a firm-level activity, whether it appears to be an isolated incident, or appears more systemic in that there have been several occurrences.
- The severity of a deficiency in terms of the impact on the engagement or the firm as a whole.
- The extent to which the cause(s) of a deficiency is apparent and the extent of actions to remediate the deficiency, i.e., the nature and extent of the causal analysis may be simpler in circumstances when the cause(s) are more apparent and the related remedial actions are uncomplicated.

A91. While paragraph 45 requires the firm to determine the cause(s) of deficiencies, the firm may also undertake a casual analysis in circumstances where there are engagements where no deficiencies were identified, in order to understand how such engagements achieved the desired level of quality.

A92. Performing a causal analysis requires those performing the assessment to apply judgment based on the evidence available. The firm's process for identifying the cause(s) of deficiencies may include:

- Identifying those responsible for performing the causal analysis, and establishing their competency to do so, including providing training on how to effectively identify the cause(s).
- Determining the nature, timing and extent of the causal analysis.
- Conducting interviews of engagement teams and others, in order to gain insight into what may have caused the deficiency.
- Evaluating the evidence and other information available and identifying the cause(s) based on such evidence.

A93. The underlying cause(s) of deficiencies may relate to a variety of factors and there may be many causes that relate to a particular deficiency. For example, deficiencies may arise as a result of:

- Matters related to firm leadership, for example, the culture of the firm, its organization and structure.
- The firm's information and communication, for example, the firm fails to establish policies or procedures that facilitate the communication of information relevant to the firm's system of quality management with the relevant parties.
- Quality objectives, risks to the quality objectives or responses to address the risks, for example, a risk to a quality objective is not identified by the firm or the firm's response to address a particular risk is inappropriate.
- Resources to support the firm's quality management or engagement teams, for example, an outdated methodology, or absence of technical support.
- Appraisal and reward systems, for example, incentives established for firm personnel that promote financial considerations to the detriment of quality.
- Consultation on difficult issues, or differences of opinion, for example, the firm culture does not promote consultation on difficult issues or the firm's process for addressing differences of opinion is not clear or well established.
- The acceptance and continuance of clients, for example, the firm accepts a client who lacks integrity or the firm accepts an engagement but does not have the capability to perform the engagement.
- The knowledge, skills and experience of firm personnel, for example, engagement team members have insufficient knowledge of the firm's methodology due to a lack of training or the firm does not provide engagement teams with experts.
- The behavior of firm personnel, i.e., the values, ethics and attitudes of firm personnel, for example, firm personnel knowingly breach the firm's policies or procedures or disregard professional standards.
- The time and resources allocated to perform the engagement, including when the work is performed.
- Engagement performance issues, for example, engagement team members do not effectively interact with others involved in the audit, e.g., in the case of a group audit.
- Interactions with management and those charged with governance, for example, there is an absence of cooperation and open dialogue with management and those charged with governance, or the engagement team fails to discuss their needs with management and agree an appropriate timetable.
- Contextual factors, including broader cultural factors and talent retention, for example, the firm operates in a jurisdiction where cultural expectations prevent less experienced engagement team members from challenging individuals with more authority (e.g., the engagement partner or client management).

A94. Identifying a cause(s) that is sufficiently specific supports the firm's process for appropriately remediating deficiencies and achieving the overall objective of the system of quality management.

For example, it may be identified that an engagement team lacked the appropriate application of professional skepticism, however the underlying cause may relate to the cultural environment whereby engagement team members typically do not challenge individuals with more authority.

Evaluating the effect of deficiencies (Ref: Para. 46)

A95. When deficiencies are identified, there is an indication that aspects of the firm's system of quality management are not designed effectively or are not functioning as intended. Accordingly, in evaluating the effect of the deficiencies, the firm considers the continued relevance of the firm's quality objectives, whether all quality risks have been identified and appropriately assessed, and whether the responses to quality risks remain appropriate. Paragraphs A52, A57 and A70 indicate that the frequency of the firm's consideration of the continued relevance of the quality objectives or whether all relevant quality objectives have been identified and the appropriateness of the quality risks and responses depends on the rate of changes in the factors and circumstances affecting the firm, the timing of when other information becomes available to the firm and the urgency of responding to such changes or information in the context of the firm's system of quality management.

Implementing appropriate remedial actions (Ref: Para. 47)

A96. The remedial actions are responsive to the cause(s) identified, for example, if the cause relates to the firm having insufficient time and resources to perform the engagement, the remedial actions may include implementing additional resources or withdrawing from engagements. The nature, timing and extent of remedial actions may depend on a variety of other factors, including:

- The extent of the impact of the cause(s), for example, whether it relates to a certain category of engagements, or is more pervasive throughout the firm. In some circumstances, the firm may determine through the causal analysis that a deficiency is not significant, or is an isolated incident, and accordingly no remedial actions are necessary or urgent.
- The severity of the cause(s) in the context of the firm's overall quality objectives and therefore the urgency in which it needs to be addressed.
- The effectiveness of the remedial actions in addressing the cause(s), for example, the firm may need to implement more than one remedial action in order to effectively address the cause(s), or may need to implement remedial actions as interim measures until such time as the firm is able to implement the most effective remedial actions.

Assessing the Effectiveness of the Monitoring and Remediation Process (Ref: Para. 48)

A97. Monitoring the effectiveness of the remedial actions might result in the need for new or improved remedial actions to address the cause(s), thereby continually improving the effectiveness of the firm's quality management.

Communicating Matters Related to Monitoring and Remediation (Ref: Para. 49)

A98. In determining the information to be communicated in relation to the firm's monitoring activities, including the nature and extent of such communication, the firm may take into consideration which information is relevant to the particular audience, including the information needs of the audience as a result of their defined roles and responsibilities. For example:

- Information communicated to engagement teams may be focused on deficiencies that have been identified at an engagement level and therefore are likely to be relevant to this audience.
- Information communicated to all firm personnel may relate to matters relevant to compliance with the firm's independence policies or procedures as such policies or procedures may apply to all firm personnel.

Communicating the causes of deficiencies increases awareness and understanding of why deficiencies occurred, which may influence the behaviors of engagement teams and firm personnel. Furthermore, communicating remedial actions on a timely basis may support the implementation of such actions.

A99. The communication of deficiencies to individuals other than the relevant engagement partners need not include an identification of the specific engagements concerned, although there may be cases where such identification may be necessary for the proper discharge of the responsibilities of the individuals other than the engagement partners.

The purpose of this document is to demonstrate the proposals of the Quality Control Task Force (QCTF) in the context of adopting a quality management approach in ISQC 1.[1]

QUALITY MANAGEMENT (FIRM LEVEL): PRESCRIBED QUALITY OBJECTIVES, QUALITY RISKS AND RESPONSES

1. This document includes the proposed prescribed quality objectives, quality risks, and responses that could be included in ISQC 1 (see paragraphs 32, 35 and 37 of **Agenda Item 2–B**). These are illustrative only and the QCTF will further consider whether additional or more enhanced requirements are necessary in response to respondents' views to the Invitation to Comment,[2] after receiving feedback from the IAASB. The QCTF is not, at this stage, seeking the IAASB's views on specific aspects of the proposed prescribed quality objectives, quality risks, and responses.

2. This document is presented in two formats (the content is identical in each of the formats):

   (a) A table format, which comprises two tables that map (i) the quality risks to the quality objectives and related responses, and (ii) the responses to the quality risks. The tables also include a reference to the extant requirements in ISQC 1 in order to illustrate how the extant requirements have been transitioned into quality risks and responses, and to confirm the retention of all of the requirements in extant ISQC 1. In some cases, the QCTF has introduced a possible new requirement or the enhancement of an extant requirement which will be further discussed with the IAASB in September 2017.

   (b) A linear format, which sets out the prescribed quality objectives, quality risks and responses.

Table Format

Quality Objectives:

QO1. The firm accepts and continues client relationships and specific engagements for which the firm is satisfied with the integrity, ethical values or diligence of management, and, where appropriate, those charged with governance, and their competence in relation to the subject matter of the engagement.

QO2. The firm accepts and continues client relationships and specific engagements for which the firm is able to perform the engagement in accordance with professional standards and applicable legal and regulatory requirements.

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[1] International Standard on Quality Control (ISQC) 1, *Quality Control for Firms that Perform Audits and Reviews of Financial Statements, and Other Assurance Engagements and Related Services Engagements*

[2] Invitation to Comment, *Enhancing Audit Quality: A Focus on Professional Skepticism, Quality Control and Group Audits*

QO3. The firm performs engagements in accordance with professional standards and applicable legal and regulatory requirements.

QO4. Reports issued by the firm or engagement partners are appropriate in the circumstances.

Quality Risks:

Quality risks	**Quality Objectives**				**Responses**	**Extant ISQC 1 reference, possible new requirement or enhancement of extant requirement**
	QO1.	QO2.	QO3.	QO4.		
QR1. The firm inappropriately accepts and continues a client relationship or specific engagement as a result of having insufficient information in relation to: (a) The competence, integrity, ethical values or diligence of management, and, where appropriate, those charged with governance, including their acknowledgement and understanding of their responsibilities in relation to the engagement; or (b) The purpose of the engagement, the underlying subject matter or the criteria to be applied in the preparation of the subject matter information and its availability to the intended users.	✓	✓	✓		R1 and R2	Enhancement of extant requirement: 26. The firm shall establish policies and procedures for the acceptance and continuance of client relationships and specific engagements, designed to provide the firm with reasonable assurance that it will only undertake or continue relationships and engagements where the firm: (a) Is competent to perform the engagement and has the capabilities, including time and resources, to do so; (b) Can comply with relevant ethical requirements; and (c) Has considered the integrity of the client, and does not have information that would lead it to conclude that the client lacks integrity.

Quality risks	**Quality Objectives**				**Responses**	**Extant ISQC 1 reference, possible new requirement or enhancement of extant requirement**
	QO1.	QO2.	QO3.	QO4.		
QR2. The judgment applied by the firm in considering the information relevant to evaluating the acceptance and continuance of a client relationship or specific engagement is inappropriate.	✓	✓			R2, R9, R11 and R13	New risk.
QR3. The firm does not communicate the identity and role of the engagement partner to key members of client management and those charged with governance.		✓			R3	30. The firm shall assign responsibility for each engagement to an engagement partner and shall establish policies and procedures requiring that: (a) The identity and role of the engagement partner are communicated to key members of client management and those charged with governance; …
QR4. The firm, its personnel and, where applicable, others subject to relevant ethical requirements (including network firm personnel) do not comply with relevant ethical requirements, including independence requirements, as a result of: (a) Insufficient knowledge of the relevant ethical requirements, including the independence requirements;	✓	✓	✓		R4, R5, R6, R7, R8 and R9	20. The firm shall establish policies and procedures designed to provide it with reasonable assurance that the firm and its personnel comply with relevant ethical requirements. 21. The firm shall establish policies and procedures designed to provide it with reasonable assurance that the firm, its personnel and, where

Quality risks	**Quality Objectives**				**Responses**	**Extant ISQC 1 reference, possible new requirement or enhancement of extant requirement**
	QO1.	QO2.	QO3.	QO4.		
(b) Insufficient knowledge of the client or the engagements undertaken in relation to the client; (c) Inadequate communication and documentation of matters related to compliance with the relevant ethical requirements, including independence requirements; (d) A failure by the firm and its personnel to: • Identify threats to compliance with the principles of the relevant ethical requirements, including readily determining whether they satisfy independence requirements; • Evaluate the threats identified; and • Take appropriate and timely action in relation to threats identified, including prompt communication of breaches of the independence requirements and further communication of such breaches within the firm in a timely manner and addressing the threats by eliminating or reducing them to an acceptable level.						applicable, others subject to independence requirements (including network firm personnel) maintain independence where required by relevant ethical requirements. 26. The firm shall establish policies and procedures for the acceptance and continuance of client relationships and specific engagements, designed to provide the firm with reasonable assurance that it will only undertake or continue relationships and engagements where the firm: … (b) Can comply with relevant ethical requirements; and …

Quality risks	**Quality Objectives**				**Responses**	**Extant ISQC 1 reference, possible new requirement or enhancement of extant requirement**
	QO1.	QO2.	QO3.	QO4.		
QR5. Reports issued by the firm or engagement partners are inappropriate as a result of the firm, its personnel and, where applicable, others subject to relevant ethical requirements (including network firm personnel) not complying with relevant ethical requirements, including independence requirements.				✓	R5, R6, R7, R8, R9, R13 and R14	20. The firm shall establish policies and procedures designed to provide it with reasonable assurance that the firm and its personnel comply with relevant ethical requirements.
QR6. Responsibility for each engagement is not assigned to an engagement partner, the responsibilities of the engagement partner are not clearly defined and communicated to that partner or the engagement partner does not have the authority to perform the role.	✓		✓		R11	30. The firm shall assign responsibility for each engagement to an engagement partner and shall establish policies and procedures requiring that: … (c) The responsibilities of the engagement partner are clearly defined and communicated to that partner.
QR7. The engagement team assigned, including the engagement partner, does not have the appropriate combination of competence and experience to perform the engagement, including knowledge or experience regarding: (a) The professional standards, including relevant ethical requirements, and applicable law or		✓	✓		R10 and R11	Enhancement of extant requirement: 29. The firm shall establish policies and procedures designed to provide it with reasonable assurance that it has sufficient personnel with the competence, capabilities, and commitment to ethical principles necessary to:

Quality risks	**Quality Objectives**				**Responses**	**Extant ISQC 1 reference, possible new requirement or enhancement of extant requirement**
	QO1.	QO2.	QO3.	QO4.		
regulation in relation to the engagement being performed; (b) The industry in which the entity operates; or (c) The underlying subject matter or the criteria to be applied in the preparation of the subject matter information.						(a) Perform engagements in accordance with professional standards and applicable legal and regulatory requirements; and (b) Enable the firm or engagement partners to issue reports that are appropriate in the circumstances. 30. The firm shall assign responsibility for each engagement to an engagement partner and shall establish policies and procedures requiring that: … (b) The engagement partner has the appropriate competence, capabilities, and authority to perform the role; and … 31. The firm shall also establish policies and procedures to assign appropriate personnel with the necessary competence, and capabilities to:

Quality risks	**Quality Objectives**				**Responses**	**Extant ISQC 1 reference, possible new requirement or enhancement of extant requirement**
	QO1.	QO2.	QO3.	QO4.		
						(a) Perform engagements in accordance with professional standards and applicable legal and regulatory requirements; and (b) Enable the firm or engagement partners to issue reports that are appropriate in the circumstances.
QR8. There is inadequate direction, supervision and review of the engagement team.		✓	✓		R11	32. The firm shall establish policies and procedures designed to provide it with reasonable assurance that engagements are performed in accordance with professional standards and applicable legal and regulatory requirements, and that the firm or the engagement partner issue reports that are appropriate in the circumstances. Such policies and procedures shall include: (a) Matters relevant to promoting consistency in the quality of engagement performance;

Quality risks	**Quality Objectives**				**Responses**	**Extant ISQC 1 reference, possible new requirement or enhancement of extant requirement**
	QO1.	QO2.	QO3.	QO4.		
						(b) Supervision responsibilities; and (c) Review responsibilities.
QR9. The engagement team does not have sufficient time to undertake the engagement.		✓	✓			31. The firm shall also establish policies and procedures to assign appropriate personnel with the necessary competence, and capabilities to: (a) Perform engagements in accordance with professional standards and applicable legal and regulatory requirements; and (b) Enable the firm or engagement partners to issue reports that are appropriate in the circumstances.
QR10. The firm does not establish, obtain or maintain sufficient and appropriate resources in order for the engagement team to effectively undertake the engagement and to promote consistency in the quality of engagement performance. *(Application material to highlight the four resources: financial, human, technological and intellectual)*		✓	✓		R10	Enhancement of extant requirement: 29. The firm shall establish policies and procedures designed to provide it with reasonable assurance that it has sufficient personnel with the competence, capabilities, and

Quality risks	**Quality Objectives**				**Responses**	**Extant ISQC 1 reference, possible new requirement or enhancement of extant requirement**
	QO1.	QO2.	QO3.	QO4.		
						commitment to ethical principles necessary to: (a) Perform engagements in accordance with professional standards and applicable legal and regulatory requirements; and (b) Enable the firm or engagement partners to issue reports that are appropriate in the circumstances.
QR11. The judgments applied in the performance of the engagement are inappropriate, including in relation to complex areas or difficult or contentious matters.		✓	✓	✓	R9, R10, R11, R12, R13 and R14	This is an overarching risk that relates to various responses that exist in extant ISQC 1, including paragraphs 34 and 43 of extant ISQC 1 (the related responses are aligned with the extant requirements below).
QR12. The firm's policies or procedures to enable the communication of concerns that originate from within or outside the firm in relation to the commitment to quality of the firm or its personnel are insufficient to capture deficiencies in the firm's system of quality management.			✓		Also refer paragraphs 26–27 of **Agenda Item 2–B**	55. The firm shall establish policies and procedures designed to provide it with reasonable assurance that it deals appropriately with: (a) Complaints and allegations that the work performed by the firm fails to comply with professional standards and

Quality risks	**Quality Objectives**				**Responses**	**Extant ISQC 1 reference, possible new requirement or enhancement of extant requirement**
	QO1.	QO2.	QO3.	QO4.		
						applicable legal and regulatory requirements; and (b) Allegations of non-compliance with the firm's system of quality control.
QR13. The firm does not respond appropriately to concerns that originate from within or outside the firm in relation to the commitment to quality of the firm or its personnel.			✓		Also refer paragraphs 26–27 of **Agenda Item 2–B**	As per above – paragraph 55 of extant ISQC 1.
QR14. Engagement files are not assembled on a timely basis after the engagement reports have been finalized, or engagement documentation is not retained for a period sufficient to meet the needs of the firm or as required by law or regulation.			✓		R15	45. The firm shall establish policies and procedures for engagement teams to complete the assembly of final engagement files on a timely basis after the engagement reports have been finalized 47. The firm shall establish policies and procedures for the retention of engagement documentation for a period sufficient to meet the needs of the firm or as required by law or regulation.
QR15. The confidentiality, safe custody, integrity, accessibility and retrievability of engagement documentation is not maintained.			✓		R16 and R17	46. The firm shall establish policies and procedures designed to maintain the confidentiality, safe custody, integrity, accessibility and

Quality risks	**Quality Objectives**				**Responses**	**Extant ISQC 1 reference, possible new requirement or enhancement of extant requirement**
	QO1.	QO2.	QO3.	QO4.		
						retrievability of engagement documentation

Responses to Quality Risks:

Responses	**Quality Risks**	**Extant ISQC 1 reference / possible new requirement**
R1. The firm shall establish policies or procedures that address obtaining or generating and communicating information in relation to: (a) The competence, integrity, ethical values or diligence of management, and, where appropriate, those charged with governance, and their acknowledgement and understanding of their responsibilities in relation to the engagement; (b) The purpose of the engagement, the underlying subject matter or the criteria to be applied in the preparation of the subject matter information and its availability to the intended users.	QR1	27. Such policies and procedures shall require: (a) The firm to obtain such information as it considers necessary in the circumstances before accepting an engagement with a new client, when deciding whether to continue an existing engagement, and when considering acceptance of a new engagement with an existing client. … (c) If issues have been identified, and the firm decides to accept or continue the client relationship or a specific engagement, the firm to document how the issues were resolved. *[documentation to be further considered as the documentation requirements in ISQC 1 are developed]*
R2. The firm shall establish policies or procedures addressing circumstances when the firm becomes aware of information after determining to accept or continue an engagement with a new or existing client, and such information may adversely affect the	QR1 and QR2	Enhancement of extant requirement: 28. The firm shall establish policies and procedures on continuing an engagement and the client relationship, addressing the circumstances where the firm obtains

Responses	Quality Risks	Extant ISQC 1 reference / possible new requirement
firm's decision to continue the engagement. Such policies or procedures shall include consideration of: (a) The professional and legal responsibilities that apply to the circumstances, including whether there is a requirement for the firm to report to the person or persons who made the appointment or, in some cases, to regulatory authorities; and (b) The possibility of withdrawing from the engagement or from both the engagement and the client relationship.		information that would have caused it to decline the engagement had that information been available earlier. Such policies and procedures shall include consideration of: (a) The professional and legal responsibilities that apply to the circumstances, including whether there is a requirement for the firm to report to the person or persons who made the appointment or, in some cases, to regulatory authorities; and (b) The possibility of withdrawing from the engagement or from both the engagement and the client relationship.
R3. The firm shall establish policies or procedures addressing the communication of the identity and role of the engagement partner to key members of client management and those charged with governance.	QR3	30. The firm shall assign responsibility for each engagement to an engagement partner and shall establish policies and procedures requiring that: (a) The identity and role of the engagement partner are communicated to key members of client management and those charged with governance; …
R4. The firm shall assign operational responsibility for compliance with the independence requirements to a partner or partners or other persons with sufficient and appropriate experience and authority in the firm to assume that responsibility.	QR4	New requirement.
R5. The firm shall establish policies or procedures that address obtaining or generating and communicating information on a	QR4 and QR5	21. …Such policies and procedures shall enable the firm to: (a) Communicate its independence requirements to its

Responses	Quality Risks	Extant ISQC 1 reference / possible new requirement
timely basis in relation to the relevant ethical requirements, including independence requirements, with: (a) Engagement teams; (b) Personnel performing functions in relation to the operation of the firm's system of quality management; and (c) Parties that are external to the firm (including network firm personnel). Such information shall include: (a) The requirements of the relevant ethical requirements, including the independence requirements so that the firm and its personnel can readily determine whether they satisfy independence requirements; (b) Information about client engagements, including the scope of services, to enable the firm and its personnel to readily determine whether the independence requirements have been met; (c) Circumstances and relationships that create a threat to independence so that appropriate and timely action can be taken; (d) Written confirmation, at least annually, of compliance with the firm's policies or procedures on independence from all firm personnel required to be independent by relevant ethical requirements;		personnel and, where applicable, others subject to them; and … 22. Such policies and procedures shall require: (a) Engagement partners to provide the firm with relevant information about client engagements, including the scope of services, to enable the firm to evaluate the overall impact, if any, on independence requirements; (b) Personnel to promptly notify the firm of circumstances and relationships that create a threat to independence so that appropriate action can be taken; and (c) The accumulation and communication of relevant information to appropriate personnel so that: (i) The firm and its personnel can readily determine whether they satisfy independence requirements; (ii) The firm can maintain and update its records relating to independence; and (iii) The firm can take appropriate action regarding identified threats to independence that are not at an acceptable level. 23. The firm shall establish policies and procedures designed to provide it with reasonable assurance that it is notified of breaches of independence requirements, and to enable it

Responses	**Quality Risks**	**Extant ISQC 1 reference / possible new requirement**
(e) The conclusions resulting from the evaluation of the threats identified and the actions to address the threats; and (f) Other relevant information to support compliance with the relevant ethical requirements.		to take appropriate actions to resolve such situations. The policies and procedures shall include requirements for: (a) Personnel to promptly notify the firm of independence breaches of which they become aware; (b) The firm to promptly communicate identified breaches of these policies and procedures to: (i) The engagement partner who, with the firm, needs to address the breach; and (ii) Other relevant personnel in the firm and, where appropriate, the network, and those subject to the independence requirements who need to take appropriate action; and (c) Prompt communication to the firm, if necessary, by the engagement partner and the other individuals referred to in subparagraph 23(b)(ii) of the actions taken to resolve the matter, so that the firm can determine whether it should take further action. 24. At least annually, the firm shall obtain written confirmation of compliance with its policies and procedures on independence from all firm personnel required to be independent by relevant ethical requirements.
R6. The firm shall establish policies or procedures that enable the firm to:	QR4 and QR5	21. …Such policies and procedures shall enable the firm to: … (b) Identify and evaluate circumstances and relationships that create threats to independence,

Responses	**Quality Risks**	**Extant ISQC 1 reference / possible new requirement**
(a) Identify threats to compliance with the principles of the relevant ethical requirements, including the independence requirements; (b) Evaluate the threats identified; (c) Address the threats by eliminating or reducing them to an acceptable level, by applying safeguards, declining the engagement or, if considered appropriate, withdrawing from the engagement, where withdrawal is possible under applicable law or regulation; (d) Evaluate whether the actions taken to address the threats to compliance with the fundamental principles have eliminated those threats or reduced them to an acceptable level; and (e) Require the engagement report not to be dated until the actions taken to address the threats have eliminated or reduced them to an acceptable level.		and to take appropriate action to eliminate those threats or reduce them to an acceptable level by applying safeguards, or, if considered appropriate, to withdraw from the engagement, where withdrawal is possible under applicable law or regulation. 22. Such policies and procedures shall require: … (c) The accumulation and communication of relevant information to appropriate personnel so that: … (iii) The firm can take appropriate action regarding identified threats to independence that are not at an acceptable level. 27. Such policies and procedures shall require: … (b) If a potential conflict of interest is identified in accepting an engagement from a new or an existing client, the firm to determine whether it is appropriate to accept the engagement. …
R7. The firm shall establish policies or procedures that enable the firm to promptly address breaches of the independence requirements, that include: (a) The responsibility of the engagement partner who, with the firm, needs to address the breach, and communicate	QR4 and QR5	23. The firm shall establish policies and procedures designed to provide it with reasonable assurance that it is notified of breaches of independence requirements, and to enable it to take appropriate actions to resolve such situations. The policies and procedures shall include requirements for:

Responses	Quality Risks	Extant ISQC 1 reference / possible new requirement
actions taken to resolve the matter in order that the firm is able to evaluate such actions; and (b) The responsibility of other relevant personnel in the firm and, where appropriate, the network, and those subject to the independence requirements who need to take appropriate action.		(a) Personnel to promptly notify the firm of independence breaches of which they become aware; (b) The firm to promptly communicate identified breaches of these policies and procedures to: (i) The engagement partner who, with the firm, needs to address the breach; and (ii) Other relevant personnel in the firm and, where appropriate, the network, and those subject to the independence requirements who need to take appropriate action; and (c) Prompt communication to the firm, if necessary, by the engagement partner and the other individuals referred to in subparagraph 23(b)(ii) of the actions taken to resolve the matter, so that the firm can determine whether it should take further action.
R8. The firm shall establish policies or procedures that address the long association of personnel with an audit or assurance client in compliance with relevant ethical requirements and include: (a) Criteria for determining the need for safeguards to reduce the familiarity threat to an acceptable level when using the same senior personnel on an assurance engagement over a long period of time; and (b) A requirement for the rotation of the engagement partner and the individuals responsible for engagement quality control review, and, where applicable, others subject to rotation requirements, after a specified period	QR4 and QR5	25. The firm shall establish policies and procedures: (a) Setting out criteria for determining the need for safeguards to reduce the familiarity threat to an acceptable level when using the same senior personnel on an assurance engagement over a long period of time; and (b) Requiring, for audits of financial statements of listed entities, the rotation of the engagement partner and the individuals responsible for engagement quality control review, and, where applicable, others subject to rotation

Responses	Quality Risks	Extant ISQC 1 reference / possible new requirement
in compliance with relevant ethical requirements in relation to audits of financial statements of listed entities.		requirements, after a specified period in compliance with relevant ethical requirements.
R9. The firm shall establish policies or procedures that promote appropriate consultation on difficult or contentious matters in relation compliance with the relevant ethical requirements.	QR2, QR4, QR5 and QR11	New requirement.
R10. The firm shall establish policies or procedures that address the competence and experience of firm personnel performing engagements, including: (a) Effective recruitment policies or procedures that support the selection of individuals of integrity who have the capacity to develop the competence and capabilities necessary to perform the firm's work and possess the appropriate characteristics to enable them to perform competently; (b) The professional education requirements, including continuing professional development, necessary to develop and maintain the required competence in performing engagements; and (c) Performance evaluations, compensation and promotion that incentivize the maintenance and development of the competence and experience of firm personnel performing engagements.	QR7, QR10 and QR11	31. The firm shall also establish policies and procedures to assign appropriate personnel with the necessary competence, and capabilities to: (a) Perform engagements in accordance with professional standards and applicable legal and regulatory requirements; and (b) Enable the firm or engagement partners to issue reports that are appropriate in the circumstances.
R11. The firm shall establish policies or procedures that establish the responsibility of the engagement partner in managing quality at the engagement level and includes policies or procedures addressing engagement direction, supervision	QR2, QR6, QR7, QR8 and QR11	33. The firm's review responsibility policies and procedures shall be determined on the basis that work of less experienced team members is reviewed by more experienced engagement team members.

Responses	Quality Risks	Extant ISQC 1 reference / possible new requirement
and review that shall be based on the premise that the work of less experienced team members is reviewed by more experienced engagement team members.		
R12. The firm shall establish policies or procedures that address appropriate consultation on difficult or contentious matters, that shall require: (a) The agreement by both the individual seeking consultation and the individual consulted on the conclusion resulting from such consultation; and (b) The implementation of the conclusion.	QR11	34. The firm shall establish policies and procedures designed to provide it with reasonable assurance that: (a) Appropriate consultation takes place on difficult or contentious matters; (b) Sufficient resources are available to enable appropriate consultation to take place; (c) The nature and scope of, and conclusions resulting from, such consultations are documented and are agreed by both the individual seeking consultation and the individual consulted; and (d) Conclusions resulting from consultations are implemented.
R13. The firm shall establish policies or procedures that require an engagement quality control review to be performed for: (a) Audits of financial statements of listed entities; (b) Engagements for which an engagement quality control review is required by law or regulation; and (c) Other engagements where the firm has identified a risk of a significant impact to the public or a reputational risk for the firm as a result of the engagement not being performed in accordance with professional standards and applicable legal and regulatory requirements, and	QR2, QR5 and QR11	There are various requirements in extant ISQC 1 in relation to engagement quality control reviews that are being considered by the QCTF.

Responses	Quality Risks	Extant ISQC 1 reference / possible new requirement
the issuance of the report by the firm or the engagement partner being inappropriate in the circumstances.		
R14. The firm shall establish policies or procedures that address dealing with and resolving differences of opinion that may arise within the engagement team, with the engagement quality control reviewer or with personnel performing functions in relation to the operation of the firm's system of quality management, including those who provide consultation. Such policies or procedures shall also include: (a) The implementation of the conclusions reached; and (b) The report not to be dated until the matter is resolved.	QR5 and QR11	43. The firm shall establish policies and procedures for dealing with and resolving differences of opinion within the engagement team, with those consulted and, where applicable, between the engagement partner and the engagement quality control reviewer. 44. Such policies and procedures shall require that: (a) Conclusions reached be documented and implemented; and (b) The report not be dated until the matter is resolved.
R15. The firm shall establish policies or procedures for engagement teams to complete the assembly of final engagement files on a timely basis after the engagement reports have been finalized.	QR14	45. The firm shall establish policies and procedures for engagement teams to complete the assembly of final engagement files on a timely basis after the engagement reports have been finalized
R16. The firm shall establish policies or procedures designed to maintain the confidentiality, safe custody, integrity, accessibility and retrievability of engagement documentation.	QR15	46. The firm shall establish policies and procedures designed to maintain the confidentiality, safe custody, integrity, accessibility and retrievability of engagement documentation
R17. The firm shall establish policies or procedures for the retention of engagement documentation for a period sufficient to meet the needs of the firm or as required by law or regulation.	QR15	47. The firm shall establish policies and procedures for the retention of engagement documentation for a period sufficient to meet the needs of the firm or as required by law or regulation.

Linear Format

Quality Objectives:

QO1. The firm accepts and continues client relationships and specific engagements for which the firm is satisfied with the integrity, ethical values or diligence of management, and, where appropriate, those charged with governance, and their competence in relation to the subject matter of the engagement.

QO2. The firm accepts and continues client relationships and specific engagements for which the firm is able to perform the engagement in accordance with professional standards and applicable legal and regulatory requirements.

QO3. The firm performs engagements in accordance with professional standards and applicable legal and regulatory requirements.

QO4. Reports issued by the firm or engagement partners are appropriate in the circumstances.

Quality Risks:

QR1. The firm inappropriately accepts and continues a client relationship or specific engagement as a result of having insufficient information in relation to:

(a) The competence, integrity, ethical values or diligence of management, and, where appropriate, those charged with governance, including their acknowledgement and understanding of their responsibilities in relation to the engagement; or [QO 1]

(b) The purpose of the engagement, the underlying subject matter or the criteria to be applied in the preparation of the subject matter information and its availability to the intended users. [QO1, QO2 and QO3]

QR2. The judgment applied by the firm in considering the information relevant to evaluating the acceptance and continuance of a client relationship or specific engagement is inappropriate. [QO1 and QO2]

QR3. The firm does not communicate the identity and role of the engagement partner to key members of client management and those charged with governance. [QO2]

QR4. The firm, its personnel and, where applicable, others subject to relevant ethical requirements (including network firm personnel) do not comply with relevant ethical requirements, including independence requirements, as a result of: [QO1, QO2 and QO3]

(a) Insufficient knowledge of the relevant ethical requirements, including the independence requirements;

(b) Insufficient knowledge of the client or the engagements undertaken in relation to the client;

(c) Inadequate communication and documentation of matters related to compliance with the relevant ethical requirements, including independence requirements;

(d) A failure by the firm and its personnel to:

- Identify threats to compliance with the principles of the relevant ethical requirements, including readily determining whether they satisfy independence requirements;
- Evaluate the threats identified; and

- Take appropriate and timely action in relation to threats identified, including prompt communication of breaches of the independence requirements and further communication of such breaches within the firm in a timely manner and addressing the threats by eliminating or reducing them to an acceptable level.

QR5. Reports issued by the firm or engagement partners are inappropriate as a result of the firm, its personnel and, where applicable, others subject to relevant ethical requirements (including network firm personnel) not complying with relevant ethical requirements, including independence requirements. [QO4]

QR6. Responsibility for each engagement is not assigned to an engagement partner, the responsibilities of the engagement partner are not clearly defined and communicated to that partner or the engagement partner does not have the authority to perform the role. [QO1 and QO3]

QR7. The engagement team assigned, including the engagement partner, does not have the appropriate combination of competence and experience to perform the engagement, including knowledge or experience regarding: [QO2 and QO3]

(a) The professional standards, including relevant ethical requirements, and applicable law or regulation in relation to the engagement being performed;

(b) The industry in which the entity operates; or

(c) The underlying subject matter or the criteria to be applied in the preparation of the subject matter information.

QR8. There is inadequate direction, supervision and review of the engagement team. [QO2 and QO3]

QR9. The engagement team does not have sufficient time to undertake the engagement. [QO2 and QO3]

QR10. The firm does not establish, obtain or maintain sufficient and appropriate resources in order for the engagement team to effectively undertake the engagement and to promote consistency in the quality of engagement performance. [QO2 and QO3] *(Application material to highlight the four resources: financial, human, technological and intellectual)*

QR11. The judgments applied in the performance of the engagement are inappropriate, including in relation to complex areas or difficult or contentious matters. [QO2, QO3 and QO4]

QR12. The firm's policies or procedures to enable the communication of concerns that originate from within or outside the firm in relation to the commitment to quality of the firm or its personnel are insufficient to capture deficiencies in the firm's system of quality management. [QO3]

QR13. The firm does not respond appropriately to concerns that originate from within or outside the firm in relation to the commitment to quality of the firm or its personnel. [QO3]

QR14. Engagement files are not assembled on a timely basis after the engagement reports have been finalized, or engagement documentation is not retained for a period sufficient to meet the needs of the firm or as required by law or regulation. [QO3]

QR15. The confidentiality, safe custody, integrity, accessibility and retrievability of engagement documentation is not maintained. [QO3]

Responses:

R1. The firm shall establish policies or procedures that address obtaining or generating and communicating information in relation to: [QR1]

(a) The competence, integrity, ethical values or diligence of management, and, where appropriate, those charged with governance, and their acknowledgement and understanding of their responsibilities in relation to the engagement;

(b) The purpose of the engagement, the underlying subject matter or the criteria to be applied in the preparation of the subject matter information and its availability to the intended users.

R2. The firm shall establish policies or procedures addressing circumstances when the firm becomes aware of information after determining to accept or continue an engagement with a new or existing client, and such information may adversely affect the firm's decision to continue the engagement. Such policies or procedures shall include consideration of: [QR1 and QR2]

(a) The professional and legal responsibilities that apply to the circumstances, including whether there is a requirement for the firm to report to the person or persons who made the appointment or, in some cases, to regulatory authorities; and

(b) The possibility of withdrawing from the engagement or from both the engagement and the client relationship.

R3. The firm shall establish policies or procedures addressing the communication of the identity and role of the engagement partner to key members of client management and those charged with governance. [QR3]

R4. The firm shall assign operational responsibility for compliance with the independence requirements to a partner or partners or other persons with sufficient and appropriate experience and authority in the firm to assume that responsibility. [QR4]

R5. The firm shall establish policies or procedures that address obtaining or generating and communicating information on a timely basis in relation to the relevant ethical requirements, including independence requirements, with: [QR4 and QR5]

(a) Engagement teams;

(b) Personnel performing functions in relation to the operation of the firm's system of quality management; and

(c) Parties that are external to the firm (including network firm personnel).

Such information shall include:

(a) The requirements of the relevant ethical requirements, including the independence requirements so that the firm and its personnel can readily determine whether they satisfy independence requirements;

(b) Information about client engagements, including the scope of services, to enable the firm and its personnel to readily determine whether the independence requirements have been met*;*

(c) Circumstances and relationships that create a threat to independence so that appropriate and timely action can be taken;

(d) Written confirmation, at least annually, of compliance with the firm's policies or procedures on independence from all firm personnel required to be independent by relevant ethical requirements;

(e) The conclusions resulting from the evaluation of the threats identified and the actions to address the threats; and

(f) Other relevant information to support compliance with the relevant ethical requirements.

R6. The firm shall establish policies or procedures that enable the firm to: [QR4 and QR5]

(a) Identify threats to compliance with the principles of the relevant ethical requirements, including the independence requirements;

(b) Evaluate the threats identified;

(c) Address the threats by eliminating or reducing them to an acceptable level, by applying safeguards, declining the engagement or, if considered appropriate, withdrawing from the engagement, where withdrawal is possible under applicable law or regulation;

(d) Evaluate whether the actions taken to address the threats to compliance with the fundamental principles have eliminated those threats or reduced them to an acceptable level; and

(e) Require the engagement report not to be dated until the actions taken to address the threats have eliminated or reduced them to an acceptable level.

R7. The firm shall establish policies or procedures that enable the firm to promptly address breaches of the independence requirements that include: [QR4 and QR5]

(a) The responsibility of the engagement partner who, with the firm, needs to address the breach, and communicate actions taken to resolve the matter in order that the firm is able to evaluate such actions; and

(b) The responsibility of other relevant personnel in the firm and, where appropriate, the network, and those subject to the independence requirements who need to take appropriate action.

R8. The firm shall establish policies or procedures that address the long association of personnel with an audit or assurance client in compliance with relevant ethical requirements and include: [QR4 and QR5]

(a) Criteria for determining the need for safeguards to reduce the familiarity threat to an acceptable level when using the same senior personnel on an assurance engagement over a long period of time; and

(b) A requirement for the rotation of the engagement partner and the individuals responsible for engagement quality control review, and, where applicable, others subject to rotation requirements, after a specified period in compliance with relevant ethical requirements in relation to audits of financial statements of listed entities.

R9. The firm shall establish policies or procedures that promote appropriate consultation on difficult or contentious matters in relation compliance with the relevant ethical requirements. [QR2, QR4, QR5 and QR11]

R10. The firm shall establish policies or procedures that address the competence and experience of firm personnel performing engagements, including: [QR7, QR10 and QR11]

(a) Effective recruitment policies or procedures that support the selection of individuals of integrity who have the capacity to develop the competence and capabilities necessary to perform the firm's work and possess the appropriate characteristics to enable them to perform competently;

(b) The professional education requirements, including continuing professional development, necessary to develop and maintain the required competence in performing engagements; and

(c) Performance evaluations, compensation and promotion that incentivize the maintenance and development of the competence and experience of firm personnel performing engagements.

R11. The firm shall establish policies or procedures that establish the responsibility of the engagement partner in managing quality at the engagement level and includes policies or procedures addressing engagement direction, supervision and review that shall be based on the premise that the work of less experienced team members is reviewed by more experienced engagement team members. [QR2, QR6, QR7, QR8 and QR11]

R12. The firm shall establish policies or procedures that address appropriate consultation on difficult or contentious matters that shall require: [QR11]

(a) The agreement by both the individual seeking consultation and the individual consulted on the conclusion resulting from such consultation; and

(b) The implementation of the conclusion.

R13. The firm shall establish policies or procedures that require an engagement quality control review to be performed for: [QR2, QR5 and QR11]

(a) Audits of financial statements of listed entities;

(b) Engagements for which an engagement quality control review is required by law or regulation; and

(c) Other engagements where the firm has identified a risk of a significant impact to the public or a reputational risk for the firm as a result of the engagement not being performed in accordance with professional standards and applicable legal and regulatory requirements, and the issuance of the report by the firm or the engagement partner being inappropriate in the circumstances.

R14. The firm shall establish policies or procedures that address dealing with and resolving differences of opinion that may arise within the engagement team, with the engagement quality control reviewer or with personnel performing functions in relation to the operation of the firm's system of quality management, including those who provide consultation. Such policies or procedures shall also include: [QR5 and QR11]

(a) The implementation of the conclusions reached; and

(b) The report not to be dated until the matter is resolved.

R15. The firm shall establish policies or procedures for engagement teams to complete the assembly of final engagement files on a timely basis after the engagement reports have been finalized. [QR14]

R16. The firm shall establish policies or procedures designed to maintain the confidentiality, safe custody, integrity, accessibility and retrievability of engagement documentation. [QR15]

R17. The firm shall establish policies or procedures for the retention of engagement documentation for a period sufficient to meet the needs of the firm or as required by law or regulation. [QR15]

QUALITY MANAGEMENT (FIRM LEVEL): TRACKING DOCUMENT OF REQUIREMENTS IN EXTANT ISQC 1[1] TO NEW PROPOSALS

This document compares the requirements in extant ISQC 1 to the proposed requirements in **Agenda Item 2–B** and **Agenda Item 2–C**. It is noted that the proposed prescribed quality objectives, quality risks, and responses in **Agenda Item 2–C** are illustrative only and the Quality Control Task Force (QCTF) will further consider whether additional or more enhanced requirements are necessary. This includes an analysis of whether the requirements in extant ISQC 1 have been fully addressed in the proposed revisions.

Extant ISQC 1		Proposals in Agenda Item 2–B and Agenda Item 2–C	
Para. Ref	**Paragraph**	**Para. Ref**	**Paragraph**
Introduction **Scope of this ISQC**		**Introduction** **Scope of this ISQC**	
1	This International Standard on Quality Control (ISQC) deals with a firm's responsibilities for its system of quality control for audits and reviews of financial statements, and other assurance and related services engagements. This ISQC is to be read in conjunction with relevant ethical requirements.	1	This International Standard on Quality Control (ISQC) deals with a firm's responsibilities for its system of quality management and applies to all firms of professional accountants who perform audits and reviews of financial statements, and other assurance and related services engagements. This ISQC sets forth requirements and guidance for the design, implementation and operation of the firm's system of quality management.
2	Other pronouncements of the International Auditing and Assurance Standards Board (IAASB) set out additional standards and guidance on the responsibilities of firm personnel regarding quality control procedures for specific types of engagements. ISA 220,[2] for example, deals with quality control procedures for audits of financial statements.	2	Other pronouncements of the International Auditing and Assurance Standards Board (IAASB) set out additional standards and guidance on the responsibilities of firm personnel regarding quality management for specific types of

[1] International Standard on Quality Control (ISQC) 1, *Quality Control for Firms that Perform Audits and Reviews of Financial Statements, and Other Assurance Engagements and Related Services Engagements*

[2] ISA 220, *Quality Control for an Audit of Financial Statements*

Extant ISQC 1		Proposals in Agenda Item 2–B and Agenda Item 2–C	
Para. Ref	**Paragraph**	**Para. Ref**	**Paragraph**
			engagements. ISA 220,[3] for example, deals with quality management for audits of financial statements. Law, regulation or relevant ethical requirements may also establish additional responsibilities for the firm in relation to quality management beyond those described in this ISQC.
			The Firm's System of Quality Management
3	A system of quality control consists of policies designed to achieve the objective set out in paragraph 11 and the procedures necessary to implement and monitor compliance with those policies.	3	A firm's system of quality management supports the firm in complying with professional standards and applicable legal and regulatory requirements and issuing reports that are appropriate in the circumstances. A firm's system of quality management comprises the following components: (a) Governance and leadership, including the organization, culture and strategy of the firm. (Ref. Para A1) (b) Information and communication, together with documentation of the firm's system of quality management. (Ref. Para A2) (c) The quality management process, which is the process by which the firm establishes its quality objectives, identifies and assesses quality risks to meeting those objectives, designs and implements responses to those quality risks, monitors its system of quality management and implements remedial actions to address identified deficiencies. (Ref. Para A3–A4)
		4	In order for the system of quality management to properly function, these components operate in conjunction with each

[3] ISA 220, *Quality Control for an Audit of Financial Statements*

Extant ISQC 1		Proposals in Agenda Item 2–B and Agenda Item 2–C	
Para. Ref	**Paragraph**	**Para. Ref**	**Paragraph**
			other and are interrelated to form the system of quality management.
		5	This ISQC establishes governance principles in relation to quality that provide the basis for the design, implementation and operation of the firm's system of quality management. The firm is required to implement actions to address these principles, which include the culture of the firm, the responsibility and accountability of firm leadership, the organization of the firm and the firm's consideration of its stakeholders. (Ref. Para A1)
		6	The quality management process assists the firm in tailoring the system of quality management according to the circumstances of the firm, through establishing quality objectives that are specific to the firm and identifying the risks that, individually or in combination, may adversely affect the firm's ability to achieve its quality objectives. This enables the firm to design and implement responses that are responsive to the quality risks, thereby promoting the effective use of the firm's resources and the effective management of quality. Factors that may affect the firm's system of quality management include, for example, the size and operating characteristics of the firm and whether it is part of a network, the types of services the firm provides, the industries in which it operates, or the nature of the entities to which those services are provided. (Ref. Para A3–A4)
		7	This ISQC includes quality objectives that form the basis for the quality objectives established by the firm, i.e., the firm identifies specific quality objectives relevant to the firm's circumstances, based on the quality objectives set out in the standard. The firm identifies quality risks in relation to such quality objectives,

Extant ISQC 1		Proposals in Agenda Item 2–B and Agenda Item 2–C	
Para. Ref	**Paragraph**	**Para. Ref**	**Paragraph**
			including the quality risks set out in this ISQC that are relevant to all firms. Furthermore, this ISQC includes responses that firms are required to implement to address the quality risks set out in this standard, however such responses may not fully address the quality risks, including due to the circumstances of the firm, and the firm may need to design and implement additional responses. (Ref. Para A4)
		8	Quality management is a continuous, dynamic process that involves an ongoing consideration of the relevance and appropriateness of the firm's system of quality management. Changes in the circumstances affecting the firm (e.g., the types of services the firm provides or the nature of the entities to which those services are provided) or other information (e.g., the results of the firm's monitoring activities or information received through the firm's whistleblowing program) may indicate the need for the firm to consider the continued relevance and appropriateness of its system of quality management and modify it, as necessary.
Authority of this ISQC		**Authority of this ISQC**	
4	This ISQC applies to all firms of professional accountants in respect of audits and reviews of financial statements, and other assurance and related services engagements. The nature and extent of the policies and procedures developed by an individual firm to comply with this ISQC will depend on various factors such as the size and operating characteristics of the firm, and whether it is part of a network.	9	This ISQC applies to all firms of professional accountants in respect of audits and reviews of financial statements, and other assurance and related services engagements.

Extant ISQC 1		Proposals in Agenda Item 2–B and Agenda Item 2–C	
Para. Ref	**Paragraph**	**Para. Ref**	**Paragraph**
5	This ISQC contains the objective of the firm in following the ISQC, and requirements designed to enable the firm to meet that stated objective. In addition, it contains related guidance in the form of application and other explanatory material, as discussed further in paragraph 8, and introductory material that provides context relevant to a proper understanding of the ISQC, and definitions.	10	This ISQC contains the objective of the firm in following the ISQC, and requirements designed to enable the firm to meet that stated objective. In addition, it contains related guidance in the form of application and other explanatory material, as discussed further in paragraph 13, and introductory material that provides context relevant to a proper understanding of the ISQC, and definitions.
6	The objective provides the context in which the requirements of this ISQC are set, and is intended to assist the firm in: • Understanding what needs to be accomplished; and • Deciding whether more needs to be done to achieve the objective.	11	The objective provides the context in which the requirements of this ISQC are set, and is intended to assist the firm in: • Understanding what needs to be accomplished; and • Determining what needs to be done to achieve the objective.
7	The requirements of this ISQC are expressed using "shall."	12	The requirements of this ISQC are expressed using "shall."
8	Where 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 of policies and procedures that may be appropriate in the circumstances. While 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 ISQC. Where appropriate, additional considerations specific to public sector audit organizations or smaller firms are included within	13	Where 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 may be appropriate in the circumstances. While 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 ISQC. Where appropriate, additional considerations specific to public sector audit organizations or smaller firms are included within

Extant ISQC 1		Proposals in Agenda Item 2–B and Agenda Item 2–C	
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	the application and other explanatory material. These additional considerations assist in the application of the requirements in this ISQC. They do not, however, limit or reduce the responsibility of the firm to apply and comply with the requirements in this ISQC.		the application and other explanatory material. These additional considerations assist in the application of the requirements in this ISQC. They do not, however, limit or reduce the responsibility of the firm to apply and comply with the requirements in this ISQC.
9	This ISQC includes, under the heading "Definitions," a description of the meanings attributed to certain terms for purposes of this ISQC. These are provided to assist in the consistent application and interpretation of this ISQC, 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 Control, Auditing, Review, Other Assurance, and Related Services Pronouncements* published by IFAC includes the terms defined in this ISQC. It also includes descriptions of other terms found in this ISQC to assist in common and consistent interpretation and translation.	14	This ISQC includes, under the heading "Definitions," a description of the meanings attributed to certain terms for purposes of this ISQC. These are provided to assist in the consistent application and interpretation of this ISQC, 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 Control, Auditing, Review, Other Assurance, and Related Services Pronouncements* published by IFAC includes the terms defined in this ISQC. It also includes descriptions of other terms found in this ISQC to assist in common and consistent interpretation and translation.
Effective Date		**Effective Date**	
10	Systems of quality control in compliance with this ISQC are required to be established by December 15, 2009.	15	Systems of quality management in compliance with this ISQC are required to be established by December 15, 20XX.
Objective		**Objective**	
11	The objective of the firm is to establish and maintain a system of quality control to provide it with reasonable assurance that:	16	The objective of the firm is to establish and maintain a system of quality management to provide the firm with reasonable assurance that:

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Para. Ref	**Paragraph**	**Para. Ref**	**Paragraph**
	(a) The firm and its personnel comply with professional standards and applicable legal and regulatory requirements; and (b) Reports issued by the firm or engagement partners are appropriate in the circumstances.		(a) The firm and its personnel comply with professional standards and applicable legal and regulatory requirements; and (b) Reports issued by the firm or engagement partners are appropriate in the circumstances.
Definitions		**Definitions**	
12	In this ISQC, the following terms have the meanings attributed below:	17	In this ISQC, the following terms have the meanings attributed below:
			(a) Causal analysis – A process for identifying the underlying cause(s) of an identified deficiency, in order that the underlying cause(s) can be appropriately addressed by the firm.
	(a) Date of report – The date selected by the practitioner to date the report.		(b) Date of report – The date selected by the practitioner to date the report.
			(c) Deficiency in the firm's system of quality management – [Placeholder for further consideration]
	(b) Engagement documentation – The record of work performed, results obtained, and conclusions the practitioner reached (terms such as "working papers" or "workpapers" are sometimes used).		(d) 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).
	(c) Engagement partner[4] – The partner or other person in the firm who is responsible for the engagement and its		(e) Engagement partner[5] – The partner or other person in the firm who is responsible for the engagement and its

[4] "Engagement partner," "partner," and "firm" should be read as referring to their public sector equivalents where relevant.

[5] "Engagement partner," "partner," and "firm" should be read as referring to their public sector equivalents where relevant.

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	performance, and for the report that is issued on behalf of the firm, and who, where required, has the appropriate authority from a professional, legal or regulatory body.		performance, and for the report that is issued on behalf of the firm, and who, where required, has the appropriate authority from a professional, legal or regulatory body.
	(d) Engagement quality control review – A process designed to provide an objective evaluation, on or before the date of the report, of the significant judgments the engagement team made and the conclusions it reached in formulating the report. The engagement quality control review process is 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.		(f) Engagement quality control review – [TO BE UPDATED]
	(e) Engagement quality control reviewer – A partner, other person in the firm, suitably qualified external person, or a team made up of such individuals, none of whom is part of the engagement team, with sufficient and appropriate experience and authority to objectively evaluate the significant judgments the engagement team made and the conclusions it reached in formulating the report.		(g) Engagement quality control reviewer – [To be updated]
	(f) Engagement team – All partners and staff performing the engagement, and any individuals engaged by the firm or a network firm who perform procedures on the engagement. This excludes an auditor's external expert engaged by the firm or by a network firm. The term "engagement team" also excludes individuals within the client's internal audit function who provide direct assistance on an audit engagement when the external		(h) Engagement team – All partners and staff performing the engagement, and any individuals engaged by the firm or a network firm who perform procedures on the engagement. This excludes an auditor's external expert engaged by the firm or by a network firm. The term "engagement team" also excludes individuals within the client's internal audit function who provide direct assistance on an audit engagement when the external

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	auditor complies with the requirements of ISA 610 (Revised 2013).[6]		auditor complies with the requirements of ISA 610 (Revised 2013).[7]
			(i) External inspections – Inspections of the firm's system of quality management or engagements performed by the firm that are undertaken by an external oversight authority.
	(g) Firm – A sole practitioner, partnership or corporation or other entity of professional accountants.		(j) Firm – A sole practitioner, partnership or corporation or other entity of professional accountants
	(h) Inspection – In relation to completed engagements, procedures designed to provide evidence of compliance by engagement teams with the firm's quality control policies and procedures.		*[The QCTF agreed that this definition should not be retained as inspections may be broader than inspection of completed engagements, and this definition created a conflict with the meaning of the term inspections used in other contexts. For example, inspections undertaken by an external oversight authority may also include inspections of the overall system of quality management.]*
	(i) 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.		(k) 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.
	(j) Monitoring – A process comprising an ongoing consideration and evaluation of the firm's system of quality control, including a periodic inspection of a selection of completed engagements, designed to		(l) Monitoring – A process comprising ongoing and periodic evaluations of whether the firm's system of quality management provides the firm with reasonable assurance that its overall objectives have been achieved.

[6] ISA 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 assistances is restricted to situations where it is permitted.

[7] ISA 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 assistances is restricted to situations where it is permitted.

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Para. Ref	**Paragraph**	**Para. Ref**	**Paragraph**
	provide the firm with reasonable assurance that its system of quality control is operating effectively.		
	(k) Network firm – A firm or entity that belongs to a network.		(m) Network firm – A firm or entity that belongs to a network
	(l) Network – A larger structure: (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 control policies and procedures, common business strategy, the use of a common brand name, or a significant part of professional resources.		(n) Network – A larger structure: (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 control policies and procedures, common business strategy, the use of a common brand name, or a significant part of professional resources.
	(m) Partner – Any individual with authority to bind the firm with respect to the performance of a professional services engagement.		(o) Partner – Any individual with authority to bind the firm with respect to the performance of a professional services engagement.
	(n) Personnel – Partners and staff.		(p) Personnel – Partners and staff. [To be considered as "staff" includes only professional staff]
	(o) Professional standards – IAASB Engagement Standards, as defined in the IAASB's *Preface to the International Quality Control, Auditing, Review, Other Assurance and Related Services Pronouncements*, and relevant ethical requirements.		(q) Professional standards – IAASB Engagement Standards, as defined in the IAASB's *Preface to the International Quality Control, Auditing, Review, Other Assurance and Related Services Pronouncements*, and relevant ethical requirements.
			(r) Quality objectives – The objectives established by the firm to achieve the firm's overall objective for the firm's system of quality management.

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Para. Ref	**Paragraph**	**Para. Ref**	**Paragraph**
			(s) Quality risk – A risk that, individually or in combination, could reasonably have an adverse impact on the firm's ability to achieve its quality objectives. [To be further considered in conjunction with the ISA 220 Task Force]
	(p) Reasonable assurance – In the context of this ISQC, a high, but not absolute, level of assurance.		(t) Reasonable assurance – In the context of this ISQC, a high, but not absolute, level of assurance. (Ref. Para A5–A6)
	(q) Relevant ethical requirements – Ethical requirements to which the engagement team and engagement quality control reviewer are subject, which ordinarily comprise Parts A and B of the International Ethics Standards Board for Accountants' *Code of Ethics for Professional Accountants* (IESBA Code) together with national requirements that are more restrictive.		(u) Relevant ethical requirements – [To be considered in the context of the IESBA's Restructure Project and whether for purposes of ISQC 1 this should relate to all staff] Ethical requirements to which the engagement team and engagement quality control reviewer are subject, which ordinarily comprise Parts A and B of the International Ethics Standards Board for Accountants' *Code of Ethics for Professional Accountants* (IESBA Code) together with national requirements that are more restrictive.
			(v) Remediation – Corrective actions implemented by the firm to address deficiencies identified in the firm's system of quality management.
			(w) Response – The firm's actions to address a quality risk, including policies or procedures.
	(r) Staff – Professionals, other than partners, including any experts the firm employs.		(x) Staff – Professionals, other than partners, including any experts the firm employs.
	(s) Suitably qualified external person – An individual outside the firm with the competence and capabilities to act as an engagement partner, for example, a partner of another		(y) Suitably qualified external person – [To be considered in context of how this term has been proposed in relation to engagement quality control reviews, i.e., the engagement

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	firm, or an employee (with appropriate experience) of either a professional accountancy body whose members may perform audits and reviews of historical financial information, or other assurance or related services engagements, or of an organization that provides relevant quality control services.		quality control reviewer does not need to have the competence and capabilities to act as engagement partner] An individual outside the firm with the competence and capabilities to act as an engagement partner, for example, a partner of another firm, or an employee (with appropriate experience) of either a professional accountancy body whose members may perform audits and reviews of historical financial information, or other assurance or related services engagements, or of an organization that provides relevant quality control services.
Requirements **Applying, and Complying with, Relevant Requirements**		**Requirements** **Applying, and Complying with, Relevant Requirements**	
13	Personnel within the firm responsible for establishing and maintaining the firm's system of quality control shall have an understanding of the entire text of this ISQC, including its application and other explanatory material, to understand its objective and to apply its requirements properly.	18	Those assigned ultimate responsibility and accountability for quality, and person(s) within the firm with operational responsibility for the firm's system of quality management, shall have an understanding of the entire text of this ISQC, including its application and other explanatory material, to understand its objective and to apply its requirements properly.
14	The firm shall comply with each requirement of this ISQC unless, in the circumstances of the firm, the requirement is not relevant to the services provided in respect of audits and reviews of financial statements, and other assurance and related services engagements. (Ref: Para. A1)	19	The firm shall comply with each requirement of this ISQC unless, in the circumstances of the firm, the requirement is not relevant to the firm. (Ref: Para. A7)
15	The requirements are designed to enable the firm to achieve the objective stated in this ISQC. The proper application of the requirements is therefore expected to provide a sufficient basis	20	The requirements are designed to enable the firm to achieve the objective stated in this ISQC. The proper application of the

Extant ISQC 1		Proposals in Agenda Item 2–B and Agenda Item 2–C	
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	for the achievement of the objective. However, because circumstances vary widely and all such circumstances cannot be anticipated, the firm shall consider whether there are particular matters or circumstances that require the firm to establish policies and procedures in addition to those required by this ISQC to meet the stated objective.		requirements is therefore expected to provide a sufficient basis for the achievement of the objective.
Elements of a System of Quality Control		**System of Quality Management**	
16	The firm shall establish and maintain a system of quality control that includes policies and procedures that address each of the following elements: (a) Leadership responsibilities for quality within the firm. (b) Relevant ethical requirements. (c) Acceptance and continuance of client relationships and specific engagements. (d) Human resources. (e) Engagement performance. (f) Monitoring.	21	The firm shall establish and maintain a system of quality management that includes the following components: (a) Governance and leadership, including the organization, culture and strategy of the firm. (b) Information, communication and documentation. (c) A quality management process, that comprises: (i) Establishing quality objectives. (ii) Identifying and assessing quality risks. (iii) Designing and implementing responses to quality risks. (iv) Monitoring and remediation.
		Information, Communication and Documentation *Information and Communication*	
17	The firm shall document its policies and procedures and communicate them to the firm's personnel. (Ref: Para. A2–A3)	28	The firm shall obtain, or generate, and communicate appropriate information necessary to enable and support the proper functioning of the firm's system of quality management, including information: (Ref: Para. A36–A37, A42, A45 and A46)

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			(a) In relation to the firm's system of quality management that is relevant to engagement teams, in order that engagement teams have the information necessary to perform the engagement; (Ref Para. A38) (b) That is relevant to personnel performing functions in relation to the operation of the firm's system of quality management, in order that such personnel are able to fulfill their responsibilities in relation to such roles, including those who are ultimately responsible and accountable for quality; and (Ref: Para. A39–A40) (c) Exchanged with parties that are external to the firm. (Ref: Para. A41) In doing so, the firm shall establish policies or procedures that facilitate the communication of such information with relevant parties that enables the firm and relevant parties to take appropriate and timely action in relation to such information. (Ref: Para. A43–A44)
		Documentation	
		29	[Placeholder – section to be further developed]
Leadership Responsibilities for Quality within the Firm		**Governance and Leadership, including Organization, Culture and Strategy**	
18	The firm shall establish policies and procedures designed to promote an internal culture recognizing that quality is essential in performing engagements. Such policies and procedures shall require the firm's chief executive officer (or equivalent)	22	The firm shall establish governance principles in relation to quality and implement them through actions set out in this ISQC, and other actions as appropriate. Such governance principles shall include: (Ref. Para A8–A11)

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	or, if appropriate, the firm's managing board of partners (or equivalent) to assume ultimate responsibility for the firm's system of quality control. (Ref: Para. A4–A5)		(a) The firm's internal culture fosters quality, including professional and ethical values, to support the firm's public interest role; (Ref. Para A12–A15) (b) The firm is organized in a manner that supports the effective design, implementation and operation of the firm's system of quality management; (Ref. Para A16–A18, A21) (c) The firm has effective leadership with responsibility and accountability for quality; and (Ref. Para A19–A20) (d) The firm enhances stakeholder confidence in the public interest aspects of the firm's decision-making in relation to quality. (Ref. Para A26–A27)
		23	The firm shall assign ultimate responsibility and accountability for quality to the firm's chief executive officer (or equivalent) or the firm's managing board of partners (or equivalent). The person(s) assuming such responsibility and accountability shall have sufficient and appropriate experience, knowledge and capacity to assume that responsibility and: (Ref: Para. A19–A20) (a) Conduct themselves in a manner that promotes an internal culture that fosters quality, including professional and ethical values, to support the firm's public interest role, and take actions to establish and extend that culture throughout the firm; (Ref: Para. A12–A13) (b) Establish a business strategy that reflects the professional and ethical values of the firm, recognizes the need for the firm to achieve quality in all engagements, supports the firm's public interest role and recognizes that commercial

Extant ISQC 1		Proposals in Agenda Item 2–B and Agenda Item 2–C	
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			considerations do not override the quality of work performed; (Ref: Para. A14) (c) Establish an organizational structure that supports the effective design, implementation and operation of the firm's system of quality management; (Ref: Para. A16–A18, A21) (d) Establish the necessary resources to support the design, implementation and operation of the firm's system of quality management and allocate these appropriately; and (Ref: Para. A24–A25) (e) Promote the consideration of the interests and expectations of all stakeholders in formulating decisions in relation to quality. (Ref: Para. A26–A27)
19	The firm shall establish policies and procedures such that any person or persons assigned operational responsibility for the firm's system of quality control by the firm's chief executive officer or managing board of partners has sufficient and appropriate experience and ability, and the necessary authority, to assume that responsibility. (Ref: Para. A6)	24	Any person(s) that are assigned operational responsibility for the firm's system of quality management shall also have sufficient and appropriate experience, knowledge and capacity to assume that responsibility. (Ref: Para. A22–A23)
		25	The firm shall establish periodic performance evaluations that assess the effectiveness of: (a) The person(s) that are assigned ultimate responsibility or accountability for quality; and (b) Any person(s) that are assigned operational responsibility for the firm's system of quality management. The firm shall implement corrective actions to address performance issues that are identified through performance

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			evaluations and which may affect the firm's achievement of its quality objectives. (Ref: Para. A11, A28–A29)
		Quality Management Process	
		30–37	All requirements in paragraphs 30–37 are new.
Relevant Ethical Requirements			
20	The firm shall establish policies and procedures designed to provide it with reasonable assurance that the firm and its personnel comply with relevant ethical requirements. (Ref: Para. A7–A10)	QR4[8]	The firm, its personnel and, where applicable, others subject to relevant ethical requirements (including network firm personnel) do not comply with relevant ethical requirements, including independence requirements, as a result of: (a) Insufficient knowledge of the relevant ethical requirements, including the independence requirements; (b) Insufficient knowledge of the client or the engagements undertaken in relation to the client; (c) Inadequate communication and documentation of matters related to compliance with the relevant ethical requirements, including independence requirements; (d) A failure by the firm and its personnel to: • Identify threats to compliance with the principles of the relevant ethical requirements, including readily determining whether they satisfy independence requirements; • Evaluate the threats identified; and • Take appropriate and timely action in relation to threats identified, including prompt communication of

[8] Throughout this Agenda Item, "QR" and "R" refer to the quality risks and responses in Agenda Item 2–C.

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			breaches of the independence requirements and further communication of such breaches within the firm in a timely manner and addressing the threats by eliminating or reducing them to an acceptable level.
		QR5	Reports issued by the firm or engagement partners are inappropriate as a result of the firm, its personnel and, where applicable, others subject to relevant ethical requirements (including network firm personnel) not complying with relevant ethical requirements, including independence requirements.
Independence			
21	The firm shall establish policies and procedures designed to provide it with reasonable assurance that the firm, its personnel and, where applicable, others subject to independence requirements (including network firm personnel) maintain independence where required by relevant ethical requirements. Such policies and procedures shall enable the firm to: (Ref: Para. A10) (a) Communicate its independence requirements to its personnel and, where applicable, others subject to them; and (b) Identify and evaluate circumstances and relationships that create threats to independence, and to take appropriate action to eliminate those threats or reduce them to an acceptable level by applying safeguards, or, if considered appropriate, to withdraw from the engagement, where withdrawal is possible under applicable law or regulation.	QR4	The firm, its personnel and, where applicable, others subject to relevant ethical requirements (including network firm personnel) do not comply with relevant ethical requirements, including independence requirements, as a result of: (a) Insufficient knowledge of the relevant ethical requirements, including the independence requirements; (b) Insufficient knowledge of the client or the engagements undertaken in relation to the client; (c) Inadequate communication and documentation of matters related to compliance with the relevant ethical requirements, including independence requirements; (d) A failure by the firm and its personnel to: • Identify threats to compliance with the principles of the relevant ethical requirements, including readily determining whether they satisfy independence requirements;

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			• Evaluate the threats identified; and • Take appropriate and timely action in relation to threats identified, including prompt communication of breaches of the independence requirements and further communication of such breaches within the firm in a timely manner and addressing the threats by eliminating or reducing them to an acceptable level.
		R5	The firm shall establish policies or procedures that address obtaining or generating and communicating information on a timely basis in relation to the relevant ethical requirements, including independence requirements, with: (a) Engagement teams; (b) Personnel performing functions in relation to the operation of the firm's system of quality management; and (c) Parties that are external to the firm (including network firm personnel). Such information shall include: (a) The requirements of the relevant ethical requirements, including the independence requirements so that the firm and its personnel can readily determine whether they satisfy independence requirements; (b) Information about client engagements, including the scope of services, to enable the firm and its personnel to readily determine whether the independence requirements have been met;

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Para. Ref	**Paragraph**	**Para. Ref**	**Paragraph**
			(c) Circumstances and relationships that create a threat to independence so that appropriate and timely action can be taken; (d) Written confirmation, at least annually, of compliance with the firm's policies or procedures on independence from all firm personnel required to be independent by relevant ethical requirements; (e) The conclusions resulting from the evaluation of the threats identified and the actions to address the threats; and (f) Other relevant information to support compliance with the relevant ethical requirements.
		R6	See below for text.
22	Such policies and procedures shall require: (Ref: Para. A10) (a) Engagement partners to provide the firm with relevant information about client engagements, including the scope of services, to enable the firm to evaluate the overall impact, if any, on independence requirements; (b) Personnel to promptly notify the firm of circumstances and relationships that create a threat to independence so that appropriate action can be taken; and (c) The accumulation and communication of relevant information to appropriate personnel so that: (i) The firm and its personnel can readily determine whether they satisfy independence requirements;	R5	See above for text.
		R6	The firm shall establish policies or procedures that enable the firm to: (a) Identify threats to compliance with the principles of the relevant ethical requirements, including the independence requirements; (b) Evaluate the threats identified; (c) Address the threats by eliminating or reducing them to an acceptable level, by applying safeguards, declining the engagement or, if considered appropriate, withdrawing from the engagement, where withdrawal is possible under applicable law or regulation;

Extant ISQC 1		Proposals in Agenda Item 2–B and Agenda Item 2–C	
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	(ii) The firm can maintain and update its records relating to independence; and (iii) The firm can take appropriate action regarding identified threats to independence that are not at an acceptable level.		(d) Evaluate whether the actions taken to address the threats to compliance with the fundamental principles have eliminated those threats or reduced them to an acceptable level; and (e) Require the engagement report not to be dated until the actions taken to address the threats have eliminated or reduced them to an acceptable level.
23	The firm shall establish policies and procedures designed to provide it with reasonable assurance that it is notified of breaches of independence requirements, and to enable it to take appropriate actions to resolve such situations. The policies and procedures shall include requirements for: (Ref: Para. A10) (a) Personnel to promptly notify the firm of independence breaches of which they become aware; (b) The firm to promptly communicate identified breaches of these policies and procedures to: (i) The engagement partner who, with the firm, needs to address the breach; and (ii) Other relevant personnel in the firm and, where appropriate, the network, and those subject to the independence requirements who need to take appropriate action; and (c) Prompt communication to the firm, if necessary, by the engagement partner and the other individuals referred to in subparagraph 23(b)(ii) of the actions taken to resolve the matter, so that the firm can determine whether it should take further action.	R5	See above for text.
		R7	The firm shall establish policies or procedures that enable the firm to promptly address breaches of the independence requirements, that include: (a) The responsibility of the engagement partner who, with the firm, needs to address the breach, and communicate actions taken to resolve the matter in order that the firm is able to evaluate such actions; and (b) The responsibility of other relevant personnel in the firm and, where appropriate, the network, and those subject to the independence requirements who need to take appropriate action.

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Para. Ref	**Paragraph**	**Para. Ref**	**Paragraph**
24	At least annually, the firm shall obtain written confirmation of compliance with its policies and procedures on independence from all firm personnel required to be independent by relevant ethical requirements. (Ref: Para. A10–A11)	R5	See above for text.
25	The firm shall establish policies and procedures: (Ref: Para. A10) (a) Setting out criteria for determining the need for safeguards to reduce the familiarity threat to an acceptable level when using the same senior personnel on an assurance engagement over a long period of time; and (b) Requiring, for audits of financial statements of listed entities, the rotation of the engagement partner and the individuals responsible for engagement quality control review, and, where applicable, others subject to rotation requirements, after a specified period in compliance with relevant ethical requirements. (Ref: Para. A12–A17)	R8	The firm shall establish policies or procedures that address the long association of personnel with an audit or assurance client in compliance with relevant ethical requirements and include: (a) Criteria for determining the need for safeguards to reduce the familiarity threat to an acceptable level when using the same senior personnel on an assurance engagement over a long period of time; and (b) A requirement for the rotation of the engagement partner and the individuals responsible for engagement quality control review, and, where applicable, others subject to rotation requirements, after a specified period in compliance with relevant ethical requirements in relation to audits of financial statements of listed entities.
Acceptance and Continuance of Client Relationships and Specific Engagements			
26	The firm shall establish policies and procedures for the acceptance and continuance of client relationships and specific engagements, designed to provide the firm with reasonable assurance that it will only undertake or continue relationships and engagements where the firm: (a) Is competent to perform the engagement and has the	QR1	The firm inappropriately accepts and continues a client relationship or specific engagement as a result of having insufficient information in relation to: (a) The competence, integrity, ethical values or diligence of management, and, where appropriate, those charged with governance, including their acknowledgement and

Extant ISQC 1		Proposals in Agenda Item 2–B and Agenda Item 2–C	
Para. Ref	**Paragraph**	**Para. Ref**	**Paragraph**
	capabilities, including time and resources, to do so; (Ref: Para. A18, A23) (b) Can comply with relevant ethical requirements; and (c) Has considered the integrity of the client, and does not have information that would lead it to conclude that the client lacks integrity. (Ref: Para. A19–A20, A23)		understanding of their responsibilities in relation to the engagement; or (b) The purpose of the engagement, the underlying subject matter or the criteria to be applied in the preparation of the subject matter information and its availability to the intended users.
		QR4	See above for text.
27	Such policies and procedures shall require: (a) The firm to obtain such information as it considers necessary in the circumstances before accepting an engagement with a new client, when deciding whether to continue an existing engagement, and when considering acceptance of a new engagement with an existing client. (Ref: Para. A21, A23) (b) If a potential conflict of interest is identified in accepting an engagement from a new or an existing client, the firm to determine whether it is appropriate to accept the engagement. (c) If issues have been identified, and the firm decides to accept or continue the client relationship or a specific engagement, the firm to document how the issues were resolved.	R1	The firm shall establish policies or procedures that address obtaining or generating and communicating information in relation to: (a) The competence, integrity, ethical values or diligence of management, and, where appropriate, those charged with governance, and their acknowledgement and understanding of their responsibilities in relation to the engagement; (b) The purpose of the engagement, the underlying subject matter or the criteria to be applied in the preparation of the subject matter information and its availability to the intended users.
		R6	See above for text.
28	The firm shall establish policies and procedures on continuing an engagement and the client relationship, addressing the circumstances where the firm obtains information that would have caused it to decline the engagement had that information	R2	The firm shall establish policies or procedures addressing circumstances when the firm becomes aware of information after determining to accept or continue an engagement with a new or existing client, and such information may adversely affect the firm's

Extant ISQC 1		Proposals in Agenda Item 2–B and Agenda Item 2–C	
Para. Ref	**Paragraph**	**Para. Ref**	**Paragraph**
	been available earlier. Such policies and procedures shall include consideration of: (a) The professional and legal responsibilities that apply to the circumstances, including whether there is a requirement for the firm to report to the person or persons who made the appointment or, in some cases, to regulatory authorities; and (b) The possibility of withdrawing from the engagement or from both the engagement and the client relationship. (Ref: Para. A22–A23)		decision to continue the engagement. Such policies or procedures shall include consideration of: (a) The professional and legal responsibilities that apply to the circumstances, including whether there is a requirement for the firm to report to the person or persons who made the appointment or, in some cases, to regulatory authorities; and (b) The possibility of withdrawing from the engagement or from both the engagement and the client relationship.
Human Resources			
29	The firm shall establish policies and procedures designed to provide it with reasonable assurance that it has sufficient personnel with the competence, capabilities, and commitment to ethical principles necessary to: (a) Perform engagements in accordance with professional standards and applicable legal and regulatory requirements; and (b) Enable the firm or engagement partners to issue reports that are appropriate in the circumstances. (Ref: Para. A24–A29)	QR7	The engagement team assigned, including the engagement partner, does not have the appropriate combination of competence and experience to perform the engagement, including knowledge or experience regarding: (a) The professional standards, including relevant ethical requirements, and applicable law or regulation in relation to the engagement being performed; (b) The industry in which the entity operates; or (c) The underlying subject matter or the criteria to be applied in the preparation of the subject matter information.
		QR10	The firm does not establish, obtain or maintain sufficient and appropriate resources in order for the engagement team to effectively undertake the engagement and to promote consistency in the quality of engagement performance. *(Application material to*

Extant ISQC 1		Proposals in Agenda Item 2–B and Agenda Item 2–C	
Para. Ref	**Paragraph**	**Para. Ref**	**Paragraph**
			highlight the four resources: financial, human, technological and intellectual)
Assignment of Engagement Teams			
30	The firm shall assign responsibility for each engagement to an engagement partner and shall establish policies and procedures requiring that: (a) The identity and role of the engagement partner are communicated to key members of client management and those charged with governance; (b) The engagement partner has the appropriate competence, capabilities, and authority to perform the role; and (c) The responsibilities of the engagement partner are clearly defined and communicated to that partner. (Ref: Para. A30)	QR3	The firm does not communicate the identity and role of the engagement partner to key members of client management and those charged with governance.
		QR6	Responsibility for each engagement is not assigned to an engagement partner, the responsibilities of the engagement partner are not clearly defined and communicated to that partner or the engagement partner does not have the authority to perform the role.
		QR7	The engagement team assigned, including the engagement partner, does not have the appropriate combination of competence and experience to perform the engagement, including knowledge or experience regarding: (a) The professional standards, including relevant ethical requirements, and applicable law or regulation in relation to the engagement being performed; (b) The industry in which the entity operates; or (c) The underlying subject matter or the criteria to be applied in the preparation of the subject matter information.
		R3	The firm shall establish policies or procedures addressing the communication of the identity and role of the engagement partner to key members of client management and those charged with governance.

Extant ISQC 1		Proposals in Agenda Item 2–B and Agenda Item 2–C	
Para. Ref	**Paragraph**	**Para. Ref**	**Paragraph**
		R10	See below for text.
31	The firm shall also establish policies and procedures to assign appropriate personnel with the necessary competence, and capabilities to: (a) Perform engagements in accordance with professional standards and applicable legal and regulatory requirements; and (b) Enable the firm or engagement partners to issue reports that are appropriate in the circumstances. (Ref: Para. A31)	QR7	See above for text.
		QR9	The engagement team does not have sufficient time to undertake the engagement.
		R10	The firm shall establish policies or procedures that address the competence and experience of firm personnel performing engagements, including: (a) Effective recruitment policies or procedures that support the selection of individuals of integrity who have the capacity to develop the competence and capabilities necessary to perform the firm's work and possess the appropriate characteristics to enable them to perform competently; (b) The professional education requirements, including continuing professional development, necessary to develop and maintain the required competence in performing engagements; and (c) Performance evaluations, compensation and promotion that incentivize the maintenance and development of the competence and experience of firm personnel performing engagements.
Engagement Performance			
32	The firm shall establish policies and procedures designed to provide it with reasonable assurance that engagements are performed in accordance with professional standards and applicable legal and regulatory requirements, and that the firm	QR8	There is inadequate direction, supervision and review of the engagement team.

Extant ISQC 1		Proposals in Agenda Item 2–B and Agenda Item 2–C	
Para. Ref	**Paragraph**	**Para. Ref**	**Paragraph**
	or the engagement partner issue reports that are appropriate in the circumstances. Such policies and procedures shall include: (a) Matters relevant to promoting consistency in the quality of engagement performance; (Ref: Para. A32–A33) (b) Supervision responsibilities; and (Ref: Para. A34) (c) Review responsibilities. (Ref: Para. A35)		
33	The firm's review responsibility policies and procedures shall be determined on the basis that work of less experienced team members is reviewed by more experienced engagement team members.	R11	The firm shall establish policies or procedures that establish the responsibility of the engagement partner in managing quality at the engagement level and includes policies or procedures addressing engagement direction, supervision and review that shall be based on the premise that the work of less experienced team members is reviewed by more experienced engagement team members.
Consultation			
34	The firm shall establish policies and procedures designed to provide it with reasonable assurance that: (a) Appropriate consultation takes place on difficult or contentious matters; (b) Sufficient resources are available to enable appropriate consultation to take place; (c) The nature and scope of, and conclusions resulting from, such consultations are documented and are agreed by both the individual seeking consultation and the individual consulted; and (d) Conclusions resulting from consultations are	R12	The firm shall establish policies or procedures that address appropriate consultation on difficult or contentious matters, that shall require: (a) The agreement by both the individual seeking consultation and the individual consulted on the conclusion resulting from such consultation; and (b) The implementation of the conclusion.

Extant ISQC 1		Proposals in Agenda Item 2–B and Agenda Item 2–C	
Para. Ref	**Paragraph**	**Para. Ref**	**Paragraph**
	implemented. (Ref: Para. A36–A40)		
Engagement Quality Control Review			
35	The firm shall establish policies and procedures requiring, for appropriate engagements, an engagement quality control review that provides an objective evaluation of the significant judgments made by the engagement team and the conclusions reached in formulating the report. Such policies and procedures shall: (a) Require an engagement quality control review for all audits of financial statements of listed entities; (b) Set out criteria against which all other audits and reviews of historical financial information and other assurance and related services engagements shall be evaluated to determine whether an engagement quality control review should be performed; and (Ref: Para. A41) (c) Require an engagement quality control review for all engagements, if any, meeting the criteria established in compliance with subparagraph 35(b).	R13	The firm shall establish policies or procedures that require an engagement quality control review to be performed for: (a) Audits of financial statements of listed entities; (b) Engagements for which an engagement quality control review is required by law or regulation; and (c) Other engagements where the firm has identified a risk of a significant impact to the public or a reputational risk for the firm as a result of the engagement not being performed in accordance with professional standards and applicable legal and regulatory requirements, and the issuance of the report by the firm or the engagement partner being inappropriate in the circumstances.
36	The firm shall establish policies and procedures setting out the nature, timing and extent of an engagement quality control review. Such policies and procedures shall require that the engagement report not be dated until the completion of the engagement quality control review. (Ref: Para. A42–A43)		The proposals of the QCTF in relation to engagement quality control reviews were presented to the IAASB in September 2016, December 2016 and March 2017. The QCTF has included a section in Agenda Item 2–B regarding the possible development of a separate standard for engagement quality control reviews. A tracking of the extant requirements to the proposed requirements will be presented to the IAASB in the
37	The firm shall establish policies and procedures to require the engagement quality control review to include:		

Extant ISQC 1		Proposals in Agenda Item 2–B and Agenda Item 2–C	
Para. Ref	**Paragraph**	**Para. Ref**	**Paragraph**
	(a) Discussion of significant matters with the engagement partner; (b) Review of the financial statements or other subject matter information and the proposed report; (c) Review of selected engagement documentation relating to significant judgments the engagement team made and the conclusions it reached; and (d) Evaluation of the conclusions reached in formulating the report and consideration of whether the proposed report is appropriate. (Ref: Para. A44)		IAASB's next discussion in relation to engagement quality control reviews, i.e., after the June 2016 meeting.
38	For audits of financial statements of listed entities, the firm shall establish policies and procedures to require the engagement quality control review to also include consideration of the following: (a) The engagement team's evaluation of the firm's independence in relation to the specific engagement; (b) Whether appropriate consultation has taken place on matters involving differences of opinion or other difficult or contentious matters, and the conclusions arising from those consultations; and (c) Whether documentation selected for review reflects the work performed in relation to the significant judgments and supports the conclusions reached. (Ref: Para. A45–A46)		

Extant ISQC 1		Proposals in Agenda Item 2–B and Agenda Item 2–C	
Para. Ref	**Paragraph**	**Para. Ref**	**Paragraph**
Criteria for the Eligibility of Engagement Quality Control Reviewers			
39	The firm shall establish policies and procedures to address the appointment of engagement quality control reviewers and establish their eligibility through: (a) The technical qualifications required to perform the role, including the necessary experience and authority; and (Ref: Para. A47) (b) The degree to which an engagement quality control reviewer can be consulted on the engagement without compromising the reviewer's objectivity. (Ref: Para. A48)		
40	The firm shall establish policies and procedures designed to maintain the objectivity of the engagement quality control reviewer. (Ref: Para. A49–A51)		
41	The firm's policies and procedures shall provide for the replacement of the engagement quality control reviewer where the reviewer's ability to perform an objective review may be impaired.		
Documentation of the Engagement Quality Control Review			
42	The firm shall 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 on or before the date of the report; and		

Extant ISQC 1		Proposals in Agenda Item 2–B and Agenda Item 2–C	
Para. Ref	**Paragraph**	**Para. Ref**	**Paragraph**
	(c) The reviewer is not aware of any unresolved matters that would cause the reviewer to believe that the significant judgments the engagement team made and the conclusions it reached were not appropriate.		
Differences of Opinion			
43	The firm shall establish policies and procedures for dealing with and resolving differences of opinion within the engagement team, with those consulted and, where applicable, between the engagement partner and the engagement quality control reviewer. (Ref: Para. A52–A53)	R14	The firm shall establish policies or procedures that address dealing with and resolving differences of opinion that may arise within the engagement team, with the engagement quality control reviewer or with personnel performing functions in relation to the operation of the firm's system of quality management, including those who provide consultation. Such policies or procedures shall also include: (a) The implementation of the conclusions reached; and (b) The report not to be dated until the matter is resolved.
44	Such policies and procedures shall require that: (a) Conclusions reached be documented and implemented; and (b) The report not be dated until the matter is resolved.		
Engagement Documentation Completion of the assembly of final engagement files			
45	The firm shall establish policies and procedures for engagement teams to complete the assembly of final engagement files on a timely basis after the engagement reports have been finalized. (Ref: Para. A54–A55)	QR14	Engagement files are not assembled on a timely basis after the engagement reports have been finalized, or engagement documentation is not retained for a period sufficient to meet the needs of the firm or as required by law or regulation.
		R15	The firm shall establish policies or procedures for engagement teams to complete the assembly of final engagement files on a timely basis after the engagement reports have been finalized.

Extant ISQC 1		Proposals in Agenda Item 2–B and Agenda Item 2–C	
Para. Ref	**Paragraph**	**Para. Ref**	**Paragraph**
Confidentiality, safe custody, integrity, accessibility and retrievability of engagement documentation			
46	The firm shall establish policies and procedures designed to maintain the confidentiality, safe custody, integrity, accessibility and retrievability of engagement documentation. (Ref: Para. A56–A59)	QR15	The confidentiality, safe custody, integrity, accessibility and retrievability of engagement documentation is not maintained.
		R16	The firm shall establish policies or procedures designed to maintain the confidentiality, safe custody, integrity, accessibility and retrievability of engagement documentation.
Retention of engagement documentation			
47	The firm shall establish policies and procedures for the retention of engagement documentation for a period sufficient to meet the needs of the firm or as required by law or regulation. (Ref: Para. A60–A63)	QR14	Engagement files are not assembled on a timely basis after the engagement reports have been finalized, or engagement documentation is not retained for a period sufficient to meet the needs of the firm or as required by law or regulation.
		R17	The firm shall establish policies or procedures for the retention of engagement documentation for a period sufficient to meet the needs of the firm or as required by law or regulation.
Monitoring Monitoring the firm's quality control policies and procedures		*Monitoring and Remediation* Establishing a Monitoring and Remediation Process	
48	The firm shall establish a monitoring process designed to provide it with reasonable assurance that the policies and procedures relating to the system of quality control are relevant, adequate, and operating effectively. This process shall:	38	The firm shall establish a monitoring and remediation process in order to evaluate whether the firm's system of quality management provides the firm with reasonable assurance that its overall objective has been achieved. (Ref: Para. A71–A72)

Extant ISQC 1		Proposals in Agenda Item 2–B and Agenda Item 2–C	
Para. Ref	**Paragraph**	**Para. Ref**	**Paragraph**
	(a) Include an ongoing consideration and evaluation of the firm's system of quality control including, on a cyclical basis, inspection of at least one completed engagement for each engagement partner; (b) Require responsibility for the monitoring process to be assigned to a partner or partners or other persons with sufficient and appropriate experience and authority in the firm to assume that responsibility; and (c) Require that those performing the engagement or the engagement quality control review are not involved in inspecting the engagement. (Ref: Para. A64–A68)	39	The firm shall design and perform monitoring activities that are sufficient to provide the firm with an evaluation of whether the system of quality management provides the firm with reasonable assurance that the overall objective has been achieved, including whether: (Ref: Para. A73) (a) The governance principles in relation to quality have been implemented and the firm's leadership has assumed ultimate responsibility and accountability for quality; (b) The firm's information and communication policies or procedures enable and support the proper functioning of the firm's system of quality management; (c) The quality management process of the firm includes appropriate quality objectives and is appropriately identifying, assessing, and responding to the quality risks; and (d) The firm's monitoring and remediation appropriately enable the evaluation of the firm's system of quality management.
		40	The firm shall determine the scope and frequency of the monitoring activities, taking into consideration: (Ref: Para. A74–A80) (a) The design and implementation of the firm's system of quality management; (b) Changes in factors that have impacted the firm's system of quality management; (c) The results of previous monitoring activities and remedial actions, including whether the previous monitoring

Extant ISQC 1		Proposals in Agenda Item 2–B and Agenda Item 2–C	
Para. Ref	**Paragraph**	**Para. Ref**	**Paragraph**
			activities continue to be relevant in evaluating the firm's system of quality management; and (d) Other information that may suggest deficiencies exist in the firm's system of quality management, including information from external inspections that may indicate the need for the firm to conduct monitoring activities.
		41	As part of the monitoring activities, the firm shall establish policies or procedures requiring the inspection of completed engagements. Such policies or procedures shall set out criteria for the selection of completed engagements for inspection that sufficiently support the firm in its evaluation of its system of quality management. Such criteria shall include the inspection of at least one completed engagement for each engagement partner on a cyclical basis determined by the firm. (Ref: Para. A81–A83)
		42	The firm shall: (a) Assign operational responsibility for the monitoring process to a partner or partners or other persons with sufficient and appropriate experience and authority in the firm to assume that responsibility; and (b) Determine that those performing the monitoring activities have sufficient and appropriate experience, knowledge and capacity to perform the monitoring activity and are sufficiently objective from the activity subject to monitoring. (Ref: Para. A84–A85)

Extant ISQC 1		Proposals in Agenda Item 2–B and Agenda Item 2–C	
Para. Ref	**Paragraph**	**Para. Ref**	**Paragraph**
			Identifying and Remediating Identified Deficiencies
		43	The firm shall assess the results of the monitoring activities and external inspections, in order to: (Ref: Para. A86–A88) (a) Identify deficiencies in the firm's system of quality management; (b) Determine the cause of deficiencies and evaluate their effect; and (c) Implement appropriate remedial actions.
		45	The firm shall determine the cause(s) of deficiencies. The nature, timing and extent of the procedures undertaken by the firm to determine the cause(s) of deficiencies shall be determined by the firm based on the nature of the deficiencies. (Ref: Para. A89–A94)
Evaluating, Communicating and Remedying Identified Deficiencies			
49	The firm shall evaluate the effect of deficiencies noted as a result of the monitoring process and determine whether they are either: (a) Instances that do not necessarily indicate that the firm's system of quality control is insufficient to provide it with reasonable assurance that it complies with professional standards and applicable legal and regulatory requirements, and that the reports issued by the firm or engagement partners are appropriate in the circumstances; or (b) Systemic, repetitive or other significant deficiencies that require prompt corrective action.	46	The firm shall evaluate the effect(s) of deficiencies, taking into account the identified cause(s). In doing so the firm shall: (a) Determine whether the cause(s) are systemic, repetitive or other causes that require timely remedial action. (b) Consider the continued relevance of the firm's quality objectives, whether all quality risks have been identified and appropriately assessed and whether the responses to quality risks remain appropriate. (Ref: Para. A95)

Extant ISQC 1		Proposals in Agenda Item 2–B and Agenda Item 2–C	
Para. Ref	**Paragraph**	**Para. Ref**	**Paragraph**
50	The firm shall communicate to relevant engagement partners and other appropriate personnel deficiencies noted as a result of the monitoring process and recommendations for appropriate remedial action. (Ref: Para. A69)		See paragraph 49 below.
51	Recommendations for appropriate remedial actions for deficiencies noted shall include one or more of the following: (a) Taking appropriate remedial action in relation to an individual engagement or member of personnel; (b) The communication of the findings to those responsible for training and professional development; (c) Changes to the quality control policies and procedures; and (d) Disciplinary action against those who fail to comply with the policies and procedures of the firm, especially those who do so repeatedly.	47	The firm shall implement remedial actions, as appropriate, that are responsive to the cause(s) of deficiencies and the related effect. (Ref: Para. A96)
		Assessing the Effectiveness of the Monitoring and Remediation Process	
		48	The firm, including those assigned ultimate responsibility and accountability for quality, shall monitor the effectiveness of the remedial actions designed and implemented to address the cause(s) and evaluate whether the remedial actions appropriately address the deficiencies identified. (Ref: Para. A97)
52	The firm shall establish policies and procedures to address cases where the results of the monitoring procedures indicate that a report may be inappropriate or that procedures were omitted during the performance of the engagement. Such policies and procedures shall require the firm to determine what further action is appropriate to comply with relevant professional standards and applicable legal and regulatory requirements and to consider whether to obtain legal advice.	44	In circumstances when a deficiency identified relates to an engagement and there is an indication that the report may be inappropriate or that procedures were omitted during the performance of the engagement, the firm shall: (a) Determine what further action is necessary to comply with relevant professional standards and applicable legal and regulatory requirements; and (b) Consider whether to obtain legal advice.
53	The firm shall communicate at least annually the results of the monitoring of its system of quality control to engagement partners and other appropriate individuals within the firm,	49	The firm shall communicate, on a timely basis or at least annually, relevant information about the results of the firm's monitoring and remediation to engagement teams, personnel

Extant ISQC 1		Proposals in Agenda Item 2–B and Agenda Item 2–C	
Para. Ref	**Paragraph**	**Para. Ref**	**Paragraph**
	including the firm's chief executive officer or, if appropriate, its managing board of partners. This communication shall be sufficient to enable the firm and these individuals to take prompt and appropriate action where necessary in accordance with their defined roles and responsibilities. Information communicated shall include the following: (a) A description of the monitoring procedures performed. (b) The conclusions drawn from the monitoring procedures. (c) Where relevant, a description of systemic, repetitive or other significant deficiencies and of the actions taken to resolve or amend those deficiencies.		performing functions in relation to the operation of the firm's system of quality management, including those who are ultimately responsible and accountable for quality, and parties that are external to the firm, as appropriate. Information communicated shall include the following: (Ref: Para. A40, A98–A99) (a) A description of the monitoring procedures performed. (b) Information about deficiencies, the causes of such deficiencies and remedial actions. (c) The conclusions drawn from monitoring and remediation.
			Considerations Relating to Networks
54	Some firms operate as part of a network and, for consistency, may implement some of their monitoring procedures on a network basis. Where firms within a network operate under common monitoring policies and procedures designed to comply with this ISQC, and these firms place reliance on such a monitoring system, the firm's policies and procedures shall require that: (a) At least annually, the network communicate the overall scope, extent and results of the monitoring process to appropriate individuals within the network firms; and (b) The network communicate promptly any identified deficiencies in the system of quality control to appropriate individuals within the relevant network firm or firms so that the necessary action can be taken,	50	[Placeholder – networks to be further considered] Some firms operate as part of a network and, for consistency, may implement some of their monitoring procedures on a network basis. Where firms within a network operate under common monitoring policies or procedures designed to comply with this ISQC, and these firms place reliance on such a monitoring system, the firm's policies or procedures shall require that: (a) At least annually, the network communicate the overall scope, extent and results of the monitoring process to appropriate individuals within the network firms; and (b) The network communicate promptly any identified deficiencies in the system of quality control to appropriate individuals within the relevant network firm or firms so that the necessary action can be taken,

Extant ISQC 1		Proposals in Agenda Item 2–B and Agenda Item 2–C	
Para. Ref	**Paragraph**	**Para. Ref**	**Paragraph**
	in order that engagement partners in the network firms can rely on the results of the monitoring process implemented within the network, unless the firms or the network advise otherwise.		in order that engagement partners in the network firms can rely on the results of the monitoring process implemented within the network, unless the firms or the network advise otherwise.
Complaints and Allegations		*Whistleblowing*	
55	The firm shall establish policies and procedures designed to provide it with reasonable assurance that it deals appropriately with: (a) Complaints and allegations that the work performed by the firm fails to comply with professional standards and applicable legal and regulatory requirements; and (b) Allegations of non-compliance with the firm's system of quality control. As part of this process, the firm shall establish clearly defined channels for firm personnel to raise any concerns in a manner that enables them to come forward without fear of reprisals. (Ref: Para. A70)	26	The firm shall establish policies or procedures that: (Ref: Para. A30–A33) (a) Enable reporting, without fear of reprisal, of concerns in relation to the commitment to quality of the firm or its personnel; and (b) Enable the investigation of concerns raised by the firm, its personnel or external parties.
		QR12	The firm's policies or procedures to enable the communication of concerns that originate from within or outside the firm in relation to the commitment to quality of the firm or its personnel are insufficient to capture deficiencies in the firm's system of quality management.
		QR13	The firm does not respond appropriately to concerns that originate from within or outside the firm in relation to the commitment to quality of the firm or its personnel.
56	If during the investigations into complaints and allegations, deficiencies in the design or operation of the firm's quality control policies and procedures or non-compliance with the firm's system of quality control by an individual or individuals are identified, the firm shall take appropriate actions as set out in paragraph 51. (Ref: Para. A71–A72)	27	If during the investigations into concerns, deficiencies in the design, implementation or operation of the firm's system of quality management are identified, the firm shall determine and evaluate the cause(s) of the deficiencies and implement remedial actions. (Ref: Para. A34–A35)

Extant ISQC 1		Proposals in Agenda Item 2–B and Agenda Item 2–C	
Para. Ref	**Paragraph**	**Para. Ref**	**Paragraph**
Documentation of the System of Quality Control		**Information, Communication and Documentation**	
57	The firm shall establish policies and procedures requiring appropriate documentation to provide evidence of the operation of each element of its system of quality control. (Ref: Para. A73–A75)		Still to be considered by the QCTF.
58	The firm shall establish policies and procedures that require retention of documentation for a period of time sufficient to permit those performing monitoring procedures to evaluate the firm's compliance with its system of quality control, or for a longer period if required by law or regulation.		Still to be considered by the QCTF.
59	The firm shall establish policies and procedures requiring documentation of complaints and allegations and the responses to them.		Still to be considered by the QCTF.

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Meeting:	IAASB
Meeting Location:	New York, USA
Meeting Dates:	June 19–22, 2017

Agenda Item
5

Quality Control—ISA 220[1]

Objectives of the Agenda Item

1. The objective of the agenda item is to obtain Board views on the matters set out in this paper, together with the proposed changes to extant ISA 220 set out in **Agenda Item 5-B**, in order to help the Task Force make progress towards developing an exposure draft of revisions to ISA 220.

ISA 220 (previously Crossover) Task Force (the 'Task Force')

2. Members of the Task Force include:
   - Megan Zietsman, IAASB Deputy Chair and Chair of the Task Force
   - Karin French, IAASB Member and Chair of the Quality Control Task Force (QCTF)
   - Rich Sharko, IAASB Member
   - Imran Vanker, IAASB Member and member of the QCTF
   - Brendan Murtagh, IAASB Member and member of the QCTF
   - Josephine Jackson, IAASB Technical Advisor and member of the QCTF and the Group Audits Task Forces
   - Annette Köhler, IAASB Member and Chair of the Professional Skepticism Working Group (correspondent member)

Activities Since the Last IAASB Discussion

3. Subsequent to the December 2016 IAASB meeting, the Task Force held two physical meetings and three teleconferences in order to develop the agenda material. The Task Force did not present any agenda items at the March 2017 IAASB meeting.

Interaction of the Project to Revise ISA 220 with Other Current IAASB Projects

4. ISA 220 is premised on the basis that the firm is subject to ISQC 1[2] or to national requirements that are at least as demanding. Therefore, the work on ISA 220 is closely aligned with the work currently being undertaken to revise ISQC 1, and the Task Forces and Staff of both projects have worked closely together in aligning the proposals. **Agenda Item 5-A** makes extensive reference to the work being done to revise ISQC 1 and therefore incorporates terms and addresses matters currently being

[1] International Standard on Auditing (ISA) 220, *Quality Control for an Audit of Financial Statements*

[2] ISQC 1, *Quality Control for Firms that Perform Audits and Reviews of Financial Statements, and Other Assurance Engagements and Related Services Engagements*

contemplated in that revision (including as it relates to the proposal to introduce a quality management approach (QMA) within ISQC 1). Accordingly, this Agenda Item should be read after having read, or in combination with reading, **Agenda Items 2-A**, **2-B**, and **2-C**.

5. Similarly, the topic of network structures has been highlighted in both the ISA 220 and ISQC 1 projects, as well as the ISA 600[3] project. The topic of networks is covered separately in **Agenda Item 4-A**.

Materials Presented

6. The agenda materials presented for the Board's consideration include **Agenda Item 5-A,** which summarizes the discussions of the ISA 220 Task Force, the key issues identified at this stage, and provides further context for the proposed enhancements and changes in **Agenda Item 5-B**. The suggestions presented reflect feedback received from the Board at its December 2016 meeting on the potential suggested enhancements and changes, feedback received in the responses to the Invitation to Comment (ITC),[4] as well as the discussions of the Task Force. A summary of the responses to the ITC relevant to the matters discussed in Agenda Item 5-A can be found in the **Supplement to Agenda Item 2**.

7. **Agenda Item 5-B** presents the extant requirements within ISA 220 and the proposed enhancements and changes to those requirements. In addition, the Task Force has given careful consideration to potential application material to support the proposed enhancements and changes. The Task Force's suggestions for additional application material are further explained in **Agenda Items 5-A and 5-B**.

Matters for IAASB Consideration

8. The IAASB is asked to provide views on the matters set out for IAASB consideration in **Agenda Item 5-A**.

Materials Presented

Agenda Item 5-A	Quality Management at the Engagement Level (ISA 220) —Issues and Discussion
Agenda Item 5-B	Quality Management at the Engagement Level Working Draft of ISA 220—Proposed Amendments to ISA 220 Requirements
Supplement to Agenda Item 2	Summary of Responses to the ITC

[3] ISA 600, Special Considerations—Audits of Group Financial Statements (Including the Work of Component Auditors)

[4] ITC, *Enhancing Audit Quality in the Public Interest: A Focus on Professional Skepticism, Quality Control and Group Audits*

Quality Management at the Engagement Level (ISA 220)[1]—Issues and Discussion

Approved minutes of the December 2016 IAASB's discussions on this topic (the last time this topic was discussed with the Board) can be found in the Appendix to this paper.

ISA 220 is premised on the basis that the firm is subject to ISQC 1[2] or to national requirements that are at least as demanding. Therefore, the work on ISA 220 is closely aligned with the work on ISQC 1. This paper makes extensive reference to the work being done to revise ISQC 1 and incorporates terms and addresses matters currently being contemplated in that revision (including as it relates to the proposal to introduce a quality management approach (QMA) within ISQC 1). Accordingly, this paper should be read after having read, or in combination with reading, Agenda Items 2-A, 2-B and 2-C.

Objectives of the Agenda Item

The objective of the agenda item is to obtain Board views on the matters set out in this paper, together with the proposed changes to extant ISA 220 set out in **Agenda Item 5-B**, in order to help the ISA 220 Task Force[3] (the "Task Force") make progress towards developing an exposure draft of revisions to ISA 220.

Background

1. A project proposal[4] that addressed the revision of the IAASB's quality control standards (ISQC 1 and ISA 220) was approved by the IAASB in December 2016. This project proposal followed outreach and extensive consultation about issues and concerns related to these standards, including:
   - Findings from the IAASB's ISA Implementation Monitoring Project, which was completed in 2013.
   - The IAASB's Invitation to Comment (ITC), *Enhancing Audit Quality: A Focus on Professional Skepticism, Quality Control and Group Audits*, which set out the issues related to quality control at the firm and engagement level, and group audits (ISA 600),[5] including highlighting areas of crossover between these standards.

[1] International Standard on Auditing (ISA) 220, *Quality Control for an Audit of Financial Statements*

[2] ISQC 1, *Quality Control for Firms that Perform Audits and Reviews of Financial Statements, and Other Assurance Engagements and Related Services Engagements*

[3] Formerly the Crossover Task Force.

[4] http://www.iaasb.org/system/files/meetings/files/20161205-IAASB_Agenda_Item_9A-GA-and-QC-Project-Proposal.pdf

[5] ISA 600, *Special Considerations—Audits of Group Financial Statements (Including the Work of Component Auditors)*

2. In December 2016, in addition to discussing matters related to finalizing the project proposal, the IAASB also discussed various matters relating to possible changes to ISA 220. In summary, Board members:

   - Supported linking the objective of the auditor to managing quality of the audit, although it was noted that more clarity about how this would be operationalized in ISA 220 was required (in particular, the IAASB noted that the distinction and interaction between a risk assessment for these purposes (i.e., risks to quality) versus the identification and assessment of the risks of material misstatement as required by ISA 315 (Revised)[6] would need to be clear);
   - Supported clarifying the engagement partner's (EP) overall responsibility and accountability for audit quality at the engagement level, while still allowing the EP to assign certain responsibilities to other members of the engagement team (ET) as necessary and appropriate;
   - Encouraged the Task Force to perform further consideration of situations where the signing partner is different from the EP who was responsible for the direction, supervision, and review of the work performed as a part of the audit;
   - Noted the need for appropriate coordination with the International Ethics Standards Board for Accountants (IESBA) relating to considerations around the definitions of EP, ET, and network firms;
   - Supported a new requirement(s) related to strengthening two-way communication among the members of the ET and those involved in the audit on a timely basis throughout the audit; and
   - Supported further consideration of how firms in networks interact, especially as relates to quality control (see **Agenda Item 4-A** for discussion about matters related to networks).

3. ISQC 1 is being revised to introduce a QMA. The matters currently being presented for discussion with the IAASB include proposals from the Quality Control Task Force (QCTF) regarding possible revisions to ISQC 1, including a revised structure. This proposed structure incorporates: (1) Governance and leadership, including organization, culture and strategy; (2) Information, communication, and documentation; and (3) The quality management process (e.g., establishing quality objectives, performing quality risk assessments, designing and implementing responses to quality risks, and monitoring and remediation)—the proposals of the QCTF are fully explained in **Agenda Items 2-A, 2-B,** and **2-C**.

4. As the various Task Forces[7] working on the revisions of the quality control standards and ISA 600 have progressed their work, the interactions and crossover between the various standards have been confirmed and further highlighted. In particular, it has been identified that many issues involve a coordinated approach to ensure that the issues are dealt with in the appropriate standard(s) and in a consistent and inter-related way. For example, ISQC 1 acknowledges that in designing responses to manage quality at the firm-level, firms may establish requirements for certain activities and procedures that are intended to be performed at the engagement level. The execution of these activities and procedures then become the responsibility of the EP, and are relevant to managing quality at the engagement level. This relationship needs to be built into ISA 220, i.e., ISA 220 needs

[6] ISA 315 (Revised), *Identifying and Assessing the Risks of Material Misstatement through Understanding the Entity and Its Environment*

[7] This includes the ISA 220 Task Force, QCTF, and the Group Audits Task Force.

to build off the principles established in ISQC 1 and deal with the issues in the context of what is relevant to managing quality at the engagement level, and the related responsibilities of the EP. In turn, ISA 600 should then build off the principles established in both ISQC 1 and ISA 220, but in the context of an audit of group financial statements where one or more component auditors may be involved.

5. One of the crossover matters related to ISQC 1, ISA 220 and ISA 600 are the various issues and concerns relating to network[8] structures. This topic is covered separately in **Agenda Item 4-A**.

6. The recommendations of the Task Force included in this agenda item have been developed based on the overall objective of embedding quality management principles and focusing on quality management at the engagement level, and taking into consideration:

   - The changes being proposed for ISQC 1.
   - The inter-relationship between firm-level actions and responses to manage quality, and what is required or expected at the engagement level, i.e., including responses to address certain requirements in ISQC 1 that are established at the firm level, but are nevertheless intended to be implemented at the engagement level and therefore as such, become matters for which the EP is responsible.

7. The Task Force acknowledges that the appropriate approach to managing quality at the engagement level can and will vary from one engagement to the next. The Task Force is of the view that the approach set out below is adaptable to audits of different sizes and complexity. It is premised on, and provides for, professional judgment being the basis for addressing the requirements, in particular those relating to determining the nature, timing and extent of direction, supervision and review by the EP (and other team members), which forms the basis for the conclusion that the EP has been sufficiently involved in the audit.

8. In debating the changes presented below, the Task Force is of the view that such revisions to ISA 220 could be expected to:

   - Enhance decision-making and improve the process of planning an audit engagement;
   - Lead to a more effective allocation and management of resources to an audit engagement by the firm, and within the audit ET;
   - Increase the probability of delivering a high-quality audit engagement;
   - Support the decision-making process by the firm on whether to accept or continue an audit, and drive more informed conclusions being reached;
   - Assist with adapting quality management at the engagement level to a wide variety of circumstances by causing more deliberate consideration of how quality may not be effectively managed for a particular engagement in the context of the elements of ISA 220, and appropriate responses should be developed;

[8] Our standards define a "network" as "a larger structure that is (a) aimed at cooperation; and (b) is clearly aimed at profit or cost-sharing or shares common ownership, control or management, common quality control policies and procedures, common business strategy, the use of a common brand name, or a significant part of professional resources." Firms that operate through such arrangements are typically referred to as a network or network firms.

- Reinforce the importance of the EP's determination of the nature, timing and extent of necessary involvement in the engagement, and provide for the ability of the approach to be applied to a wide variety of circumstances (e.g., that the requirements can be 'flexed' as appropriate in situations where there is a small, non-complex entity and when entities are larger or have more complex issues);
- Focus auditors on controls over the use of technology tools being used; and
- Encourage an enhanced understanding of (and response to) factors that may incentivize or dis-incentivize the appropriate application of professional skepticism by the ET.

9. This paper is organized into the following sections:

Section A	Interaction of ISA 220 with ISQC 1 and Other Relevant ISAs
Section B	Quality Management at the Engagement Level
Section C	The Overall Responsibility of the Engagement Partner for the Audit
Section D	The Core Elements to be Addressed on All Audits
Section E	Way Forward

10. This paper should be read in conjunction with the possible changes to ISA 220 set out in **Agenda Item 5-B**.

A. Interaction of ISA 220 with ISQC 1 and Other Relevant ISAs

11. Extant ISA 220 deals with the specific responsibilities of the auditor regarding quality control procedures for an audit of financial statements. In particular, it sets out requirements dealing with the responsibilities of the EP, and where applicable, the responsibilities of the engagement quality control reviewer. The proposed revisions to ISA 220 (set out in Sections B−D below) have been developed in light of the proposed revisions being made to ISQC 1 and are intended to help the auditor focus on quality management at the engagement level.

12. In order to meet the objectives of ISQC 1, firms establish the foundation for quality management for all engagements undertaken by the firm by identifying and addressing risks to quality, and implementing responses to those risks. The objective of ISA 220 is focused on the management of quality at the engagement level, but this objective needs to be addressed in the context of the firm's system of quality management as it relates to an audit of financial statements. ISA 220 therefore needs to demonstrate how the principles or requirements established in ISQC 1 are embedded and applied at the engagement level for audit engagements.

13. In developing the changes to ISA 220, the Task Force is of the view that the linkages and inter-relationships between quality management at the firm-level and at the engagement-level need to be strengthened and further clarified. This includes making it clear in ISA 220 that the EP has responsibility for: (i) understanding how the responses that the firm has designed to address risks to quality at the firm level are relevant to the audit engagement for which the EP is responsible; and (ii) for taking appropriate action to effectively implement the responses at the engagement level, or to

determine that they are executed as expected. The proposed changes to ISA 220 for such responsibilities are further discussed in Section C of this paper.

14. To strengthen the link to ISQC 1 for the firm's system of quality management, the Task Force therefore proposes including additional paragraphs in the introductory material in ISA 220 to highlight that ISA 220 expands on how quality management principles in ISQC 1 are applied for audits of financial statements, and through providing more context about what ISQC 1 requires for firms (see revised paragraph 1, 2, and new paragraphs 2A and 2B, in **Agenda Item 5-B** (also note the proposal to develop additional application guidance)). Furthermore, in the changes that are being proposed to the core elements of ISA 220 (further explained in Section B below), the requirements will focus the auditor on understanding what policies or procedures, or actions, the firm has in place or requires before considering what further response is necessary at the engagement level. The Task Force is of the view that the introductory paragraphs of ISA 220 need to highlight that the firm's policies or procedures form the foundation of the EP's responsibilities for managing quality, including setting out the EP's role and responsibilities in managing quality at the engagement level. These introductory paragraphs will also then support the changes being proposed in relation to what the EP is required to do in relation to each core element that is required to be addressed in managing quality at the engagement-level (described further in Sections B−D of this agenda item).

15. The Task Force has also discussed how to clarify the responsibilities of the EP. The Task Force is seeking to reiterate the fundamental premise that the EP is responsible for managing quality for an audit of financial statements, however the Task Force notes that it is not possible nor practical for the EP to personally perform ***all*** the procedures that might be relevant in addressing the requirements of ISA 220. The Task Force also believes that the EP should be ***sufficiently involved*** in the engagement in order to have a basis for demonstrating how the EP has addressed the requirements relating to managing quality at the engagement level (e.g., as demonstrated through sufficient and appropriate involvement in the direction, supervision and review of other members of the ET and others involved in the audit). The Task Force has therefore proposed including background material to this effect in the revisions to ISA 220 (see paragraph 3A in **Agenda Item 5-B**). Note that this concept is also addressed further in the proposed revisions to paragraphs 15 and 16 of extant ISA 220 – see Section D related to Engagement Performance. In developing these changes, the Task Force agreed that:

- It should be made clear that the EP may assign activities to others to assist the EP in fulfilling his or her responsibilities; however being mindful of any specific requirements of the ISAs whereby an EP may have to perform certain procedures and any firm requirements whereby certain policies or procedures are required to be addressed or performed specifically by the EP. The Task Force has considered developing application material that would include guidance, including some examples, about responsibilities that cannot be assigned.
- In each of the core elements of ISA 220, it should be made clearer what the EP's responsibilities are. The Task Force is of the view that the changes proposed in section D below, will help EPs to understand more specifically what their responsibilities are.

The Task Force has also considered the need to revisit how terminology is used throughout ISA 220, and whether revisions are needed to drive more consistent understanding and application:

- For example, use the term "engagement partner" where the requirement is addressing something that is the specific responsibility of the EP, and "auditor" where the specific procedure may be assigned to another member of the team or someone else involved in the

audit. The Task Force will further consider this approach as the revision of ISA 220 is progressed, but is preliminarily of the view that it may result in changes that are too subtle and not easily understood. The Task Force also notes that the majority of the requirements in extant ISA 220 are directed at the EP, and does not anticipate changing this in the proposed revisions.

16. The proposed revisions to ISQC 1 also strengthen the requirements in relation to obtaining or generating and communicating between the firm, ETs, personnel performing functions in relation to the firm's system of quality management, and parties that are external to the firm. As part of strengthening the linkage to ISQC 1, the Task Force is of the view that highlighting the overarching requirement for effective two-way communication in the introductory paragraphs is important (see new paragraph 2B in **Agenda Item 5-B**). Further changes related to communication, including addressing the necessary information required to be communicated and to whom, as well as highlighting the responsibilities of the EP and ET to communicate effectively and on a timely basis have also been considered by the Task Force and are discussed further in Section D below.

Matters for IAASB Consideration:

1. The IAASB is asked to share its views on the revised introductory paragraphs 2−3A in the introductory paragraphs of ISA 220 (see **Agenda Item 5-B**), in particular:
   (a) That it should be made clear that the EP may assign procedures to others to assist the EP in fulfilling his or her responsibilities.
   (b) Whether the link to ISQC 1 has been clearly made.

17. ISA 220 also interacts with activities addressed by other ISAs that are also applicable at the planning stage of an audit. It is the view of the Task Force that these interactions need to be highlighted more prominently in the introductory paragraphs as information learned from addressing requirements in other ISAs will be relevant to addressing the requirements of ISA 220. The Task Force also notes that as the audit progresses, additional information may become available that may also affect managing quality at the engagement level. The Task Force therefore proposes adding references to the following ISAs in the introductory paragraphs:

- ISA 210[9]—deals with the auditor's responsibilities in agreeing the terms of the audit engagement, including the preconditions for an audit as well as understanding if there will be limitations on the scope of the engagement.
- ISA 300[10]—Paragraph 2 of ISA 300 describes how an audit involves establishing the overall audit strategy for the engagement and developing an audit plan, and highlights ways in which adequate planning benefits the audit engagement. The matters listed in this paragraph include those that are addressed by ISA 220. Additionally, paragraphs 6 and 13 of ISA 300 addresses preliminary engagement activities and makes reference to the required procedures relating to acceptance or continuance of client relationships and the specific audit engagement, and compliance with relevant ethical requirements, all in accordance with ISA 220. Some matters set out in paragraph 8 of ISA 300 also make reference to matters that would also be considered in ISA 220 (e.g., resources necessary for the engagement). Paragraph 10 of ISA 300 deals

[9] ISA 210, *Agreeing the Terms of Audit Engagements*

[10] ISA 300, *Planning an Audit of Financial Statements*

with the need to plan the nature, timing and extent of direction and supervision of ET members and the review of their work and the related application guidance also refers back to ISA 220.

- ISA 315 (Revised)—although no specific reference is currently made to ISA 220 in ISA 315 (Revised), information relevant to managing quality at the engagement level is also relevant to the process of identifying and assessing risks of material misstatement through understanding the entity and its environment and its internal control (for example, information gathered and considered during client and engagement acceptance or continuance). Similarly, performing further audit procedures in response to the risks of material misstatement will also affect or be relevant to how quality is managed overall (for example, through a need to include individuals with particular skills or expertise in the ET, or to take a particular approach to direction and supervision for a particular area).

18. The interaction of ISA 220 with ISA 210, ISA 300 and ISA 315 (Revised) suggests that acceptance or continuance and other aspects of managing quality are not isolated from planning the audit engagement in terms of ISA 300 and ISA 315 (Revised), and that this process is not linear. The Task Force is also of the view that it is important to recognize that information obtained in fulfilling the requirements of each of the various applicable standards is not isolated, and that the understanding of the entity and its environment is applicable to more than one standard. The Task Force believes that these inter-relationships among the standards should be made clearer in ISA 220 and the other standards. In addition to the proposed amendments to the introductory paragraphs of ISA 220, conforming amendments may also be necessary to ISA 300 and ISA 315 (Revised), for example to make it clear that the requirements of the applicable ISAs may be addressed simultaneously, and involve an iterative process, and that aspects of obtaining an understanding of the entity and its environment are relevant to addressing multiple requirements within the ISAs. It is intended that application material be developed to provide examples of information that may be applicable to the various aspects of accepting or continuing the engagement and planning the audit (see revised paragraph 3B of ISA 220 in **Agenda Item 5-B**).

Matter for IAASB Consideration:

2. The IAASB is asked whether making the links to other relevant ISAs in the introductory paragraphs 3B–3D (see **Agenda Item 5-B**) is helpful for explaining the interactions between the standards, and whether additional references need to be considered to highlight interactions with any other standards.

B. Quality Management at the Engagement Level

19. The overarching objective of ISA 220 is related to the effective management of quality at the engagement level, and a key aspect is the establishment of the responsibility of the EP for the audit engagement and its performance. The responses to the ITC highlighted the need for more emphasis on, and clarity about, the responsibilities of the EP.

20. The objective of the auditor has not been substantially amended, other than revising the terminology to refer to quality management. The objective also remains consistent with the objective of ISQC 1 (See paragraph 6 of **Agenda Item 5-B)**. In revising this paragraph the Task Force also proposes that the overall objective could also more explicitly encompass “achieving” quality, i.e., noting that “managing quality” may be read by some as not necessarily encompassing a quality outcome.

However, the Task Force will continue to deliberate what the most appropriate language to achieve this objective is, as well as remain coordinated with the QCTF in this regard.

21. To be consistent with the revision of ISQC 1 to integrate a QMA, and as discussed above, the Task Force is of the view that ISA 220 should also incorporate quality management principles at the engagement level. The Task Force has extensively explored what 'quality management at the engagement level' means and how quality management principles can be introduced into ISA 220.

22. The revisions being explored in relation to ISQC 1 and extant ISA 315 (Revised) approach quality management and the audit respectively through a process that, among other things, involves identifying and assessing risks (i.e., quality risks or risks of material misstatement) and responding accordingly. The Task Force has previously considered whether and how to introduce a risk assessment process for quality management at the engagement level—an approach to managing quality at the engagement level through quality risk identification and assessment for the individual engagement was preliminarily explored with the IAASB at its December 2016 meeting (see paragraphs 46−53 of Agenda Item 8–A of the December 2016 IAASB meeting materials). The IAASB expressed caution about the proposed approach, noting the potential confusion that might be created through the introduction of yet another discrete risk assessment process at the engagement level, and questioned how such a process would align or intersect with the existing risk assessment process that is the foundation of ISA 315 (Revised) and ISA 330[11] (i.e., focused on identifying, assessing and responding to risks of material misstatement at the financial statement and assertion level). The IAASB encouraged the Task Force to further consider how quality management could be embedded at the engagement level.

23. Extant ISA 220 sets out the requirements for the aspects of quality control that are required to be addressed in an audit (i.e., the core elements of ISA 220). Each of these core elements is initially addressed by the firm in extant ISQC 1 (i.e., the 'elements of a system of quality control'), with ISA 220 setting out how these are applied specifically in audit engagements. These core elements include:

- Relevant Ethical Requirements.
- Acceptance and Continuance of Client Relationships and Audit Engagements.
- Assignment of Engagement Teams.
- Engagement Performance (including direction, supervision and performance; reviews; consultation; engagement quality control review and differences of opinion).
- Monitoring.

24. Instead of proposing the introduction of an overarching requirement to perform a quality risk assessment at the engagement level, the Task Force is of the view that building quality management into an individual audit engagement would most effectively be accomplished by embedding quality management principles into each core element of ISA 220.

25. The QCTF are exploring how the new requirements to establish quality objectives, and identify quality risks and responses can be practically applied to the quality elements in extant ISQC 1 (which are aligned with the ISA 220 core elements set out in paragraph 23 above). In developing the prescribed

[11] ISA 330, *The Auditor's Responses to Assessed Risks*

quality risks and responses, the QCTF have retained the existing requirements within the elements in ISQC 1, albeit that they have been restructured as either quality risks or responses. **Agenda Item 2-C** sets out the QCTF's initial proposals regarding the prescribed quality objectives, quality risks and responses and includes alternative forms of presentation for the IAASB to consider. As explained in paragraphs 81-82 of **Agenda Item 2-A**, the QCTF is considering whether the quality objectives, quality risks and responses should be categorized according to the elements that exist in extant ISQC 1.

26. The Task Force believe that the core elements of extant ISA 220 (as set out in paragraph 23 above) should be retained, as they are integral to an effective approach to managing quality at the engagement level. The Task Force also views the retention of the core elements as important in retaining the rigor of the extant standard. Even though the core elements may not be articulated as discretely in the revised ISQC 1, the Task Force also notes that these elements would however be established initially by a firm as part of addressing the ISQC 1 requirements (i.e., as part of implementing and operating the firm's system of quality management).

27. The Task Force has also considered, in light of the changes being made to ISQC 1, whether there are other core elements that need to be addressed at the engagement level, but is of the view that the overall core elements are complete (and consistent with what is described in extant ISQC 1 and ISA 220) and there is no need for further change. However, the Task Force believes that there are aspects of the core elements that need to be further considered and clarified. These views are reflected in the changes that have been proposed and explained further in Section D below. The Task Force will continue to monitor developments in ISQC 1, and as the changes to ISQC 1 are finalized, the Task Force will continue to consider whether the proposed approach of continuing to use the core elements in ISA 220 as the structure for the standard requires reconsideration.

28. The Task Force is of the view that the most effective way to embed quality management principles at the engagement-level is through establishing a 'four-step approach' that sets out the steps that would need to be addressed for each core element, including appropriate responses based on engagement facts and circumstances. This approach would also include an overarching requirement (or stand-back) for the EP to consider whether there is anything else that would cause quality to not be achieved for that audit engagement, and if so, to take action to implement an appropriate response.

29. As noted above, quality management at the engagement level is performed in the context of the firm's quality management system (i.e., addressing the requirements of ISQC1). The firm will have set quality objectives and identified quality risks in relation to those objectives (including risks related to audits of financial statements), and will have designed responses to those risks.

30. Accordingly, at the engagement level, for each core element and in light of the specific engagement's facts and circumstances, the EP should understand the applicable firm-level policies or procedures and consider what the firm has put in place (including what is expected at the engagement level) to address quality risks for the engagement. As well as adding more specificity about the EP's responsibilities to the various elements in ISA 220, the Task Force is of the view that applying a four-step approach that address the EP's responsibilities will help reinforce and clarify the overall responsibility of the EP for the audit.

31. Therefore, the Task Force proposes that the section of ISA 220 that sets out the EP's overall responsibilities for the engagement would be expanded to include the four-step approach, and that the approach be applied in addressing each of the core elements of ISA 220. The four-step approach

would effectively require the EP to understand, for each core element, what could go wrong such that quality would not be achieved, and to put in place actions to address those risks to quality. The four-step approach to be applied to each core element of ISA 220 would address the EP's responsibilities to:

- **Understand** what the firm's policies or procedures are that are relevant to the engagement for the core elements. This approach would:
    - Build on the firm's system of quality management required by ISQC 1 for the firm based on the firm's identification and assessment of risks to quality and the firm's responses; and
    - Focus the EP on those aspects of quality management that are relevant to the engagement, and on the EP's responsibilities for taking action in this regard at the engagement level.
- **Determine** whether the firm's policies or procedures are **sufficient and effective**[12] for that particular engagement, including understanding whether the firm's policies or procedures are effectively designed, operating as intended, and whether they are sufficient for the particular engagement, or whether incremental actions are necessary). EP's would also need to consider any impact or outcome of the responses undertaken at the firm level for the engagement (for example, the outcome of the firm's independence monitoring procedures on the engagement acceptance or continuance decision).
- **Respond** to risks to quality for the audit by taking action to address the risks to quality as appropriate and in the context of the particular element. The EP would implement the firm's policies or procedures at the engagement level, and other incremental responses as deemed necessary by the EP. Developing appropriate responses at the engagement level will involve professional judgment and the exercise of professional skepticism, and would be based on the facts and circumstances of the engagement—for example, the more complex and difficult the engagement, the more involved or detailed the response may need to be at the engagement level and the more the personal involvement of the EP may be required. The Task Force is also of the view that developing appropriate examples to be included in the application guidance would also provide an opportunity to demonstrate how professional skepticism may be applied.
- **Communicate** as appropriate with the firm (e.g., ask for more information from the firm or provide feedback to the firm where necessary), with members of the ET and others involved in the audit and with external parties as appropriate.

32. For example, the firm may identify risks to audit quality related to the challenging implications of a new accounting standard for an industry. The firm therefore establishes a requirement for audit engagements in that industry to be subject to independent reviews by an industry expert of risk assessment and planning, prior to the commencement of the planned further audit procedures. The firm includes this new requirement in its audit manual and communicates with its personnel through an announcement in its weekly technical bulletin and by highlighting the new accounting standard

[12] Assessing effectiveness would not suggest that the 'operating effectiveness' (as described in the risk assessment standards) needs be tested by each ET. Application material would be added to explain however that the EP or ET cannot just assume that the firm's response is sufficient and effective, and would provide examples of how an EP or ET can determine that firm-level policies or procedures are effective.

requirement in the technical training session that is mandatory for all audit personnel. In this case, the EP for an audit in that industry would have responsibility for understanding that the engagement is subject to the new requirement, for determining that an appropriate independent reviewer has been assigned to the engagement, for co-operating with the reviewer and for making sure that the review is complete and the related comments addressed before the ET commences with the planned audit procedures.

33. The application of the four-step approach to each of the specific core elements of 220 is discussed further in Section D below.

34. Once all core elements have been considered and addressed, the Task Force is of the view that the EP should perform a 'stand-back' evaluation on whether all of the quality risks have been addressed or whether there are any incremental risks, and take further action as appropriate. This evaluation is further discussed in paragraphs 80 to 83 below.

35. The Task Force is of the view that the four-step approach and overall stand-back, although not prescribed by the requirements addressing the elements in extant ISA 220 currently, is likely to be implicitly or explicitly applied in practice today by many firms. Such a new approach will also necessitate enhanced documentation requirements; however these will be considered by the Task Force once the Board's views on the proposed approach have been obtained. Such In addition to being helpful to the auditor in determining how the risks to quality have been identified and addressed at the engagement level, enhanced documentation requirements will also provide the appropriate basis for audit oversight bodies and other reviewers to understand how the requirements of ISA 220 have been addressed, and the objective of the standard achieved.

36. Changes to reflect the Task Force views are further described in this paper below, including initial thinking as to how the four-step approach would be reflected in the requirements to address each of the core elements and the introduction of a communication and information section. Board members should note that the proposed revisions to incorporate the four-step approach into the requirements addressing the core elements of ISA 220 represent initial thinking by the Task Force and are intended to illustrate for the board how the approach might be incorporated. The Task Force is aware that additional refinement and clarification will be necessary. In progressing its work, the Task Force will be mindful of the changes being developed in ISQC 1, and will also bear in mind the responses to the ITC. The Task Force is of the view that the proposed approach and related revisions would demonstrate the importance of proactive quality management at the engagement level, retain the current rigor in ISA 220, and also incorporate the robust changes being made in ISQC 1 to requirements for managing quality at the firm-level.

Matters for IAASB Consideration:

3. The IAASB is asked for its views on the 'objective' of the auditor as described in paragraph 20. i.e., whether the objective is to 'manage' engagement quality or 'manage and achieve' engagement quality.

4. Does the overall approach described in Section B above appropriately embed quality management principles in ISA 220, thereby effectively responding to calls for enhancing audit quality at the engagement level?

C. The Overall Responsibility of the Engagement Partner for the Audit

37. As explained above, in order to entrench quality management principles and more clearly link the EP's considerations at the engagement level to what the firm has in place, a four-step approach to guide the EP's considerations in relation to understanding what could go wrong in relation to quality for each core element would be established (see paragraphs 30−31 above). The Task Force is also of the view that an emphasis on the need for timely information and communication as part of the EP's responsibilities would also help entrench the revised requirements in ISA 220 (see further discussion relating to communication in paragraphs 42−51 below). Revised paragraph 8 in **Agenda Item 5-B** sets out the proposed overall framework that will assist the EP in achieving the objective for managing quality of the engagement. The revised requirement also makes clear that managing quality is achieved through addressing the other requirements in the standard, i.e., as they relate to the core elements.

38. In order for EPs to be able to assess risks to quality for the engagement and determine whether the responses to those risks are sufficient and effective, EPs will need to have an understanding of the entity and its environment and the circumstances of the engagement that is sufficient to be able to discharge these responsibilities. Therefore the Task Force is of the view that a new requirement should be added that sets out the requirement for the EP to have an understanding of the nature of the entity and its circumstances as the foundation for addressing the requirements of this ISA. See new paragraph 8A in **Agenda Item 5-B**. This new requirement involves designing an appropriate approach to the direction, supervision and review of the engagement, i.e., to form the basis for the conclusion that the EP's involvement has been sufficient to support the conclusion that quality has been effectively managed and achieved.

39. The Task Force proposes that application material be developed to provide guidance on the types of matters that would form the basis of the understanding referred to in new paragraph 8A, such as an understanding of the nature of the entity (e.g., whether it is a business enterprise, a public sector entity or a not-for-profit organization) and the industry in which it operates (some industries require specific expertise); the relevant applicable financial reporting framework and how it is applied to the entity (including any specific complexities that arise); the organization and structure of the entity; and applicable laws and regulations. In practice, some of this information may already have been obtained (or may be in the process of being obtained or updated) in order to meet various requirements of ISQC 1, ISA 210, ISA 300 or ISA 315 (Revised). The new requirement proposed for ISA 220 is intended to make sure that the EP has the relevant knowledge about the engagement to form the basis for designing the approach to managing and achieving quality at the engagement level and acknowledges that some of the information for the required understanding may have been obtained by others (e.g., others might have obtained relevant information in accepting or continuing the client or engagement and it is important that knowledge of such information be appropriately communicated to the EP and other team members as necessary).

40. Further, the Task Force is of the view that greater clarity around the responsibilities of the EP could be provided through new application material being included throughout the standard, such as:

    - Examples of how specific policies or procedures at the firm level may mitigate risks to quality for the engagement such that no further action may be needed at the engagement level. For example, identified risks to quality may be mitigated by firms requiring an engagement quality control (EQC) reviewer or other reviewers for certain high-risk clients, and therefore the EP

may conclude that no further reviews by individuals outside the ET are needed at the engagement level.

- Examples of engagement–specific actions to address engagement-specific risks, such as seeking consultation for an area where the firm does not specifically require consultation. For example, the entity may own assets in a jurisdiction that the ET is unfamiliar with, and an impairment test is required—the ET may want to consult with appropriate resources within the firm or in a network firm in the jurisdiction to determine that appropriate indices have been used in the related assumptions, and that the impairment assessment is appropriate in the context of the jurisdiction's environment.

Matters for IAASB Consideration:

5. The IAASB is asked for its views on:
   (a) The four-step approach to be applied in addressing each of the core elements of ISA 220 set out in paragraph 31.
   (b) Whether the core elements of ISA 220, set out in paragraph 23, are still relevant and should be retained, and whether these are complete (i.e., are there other elements or quality risks that should be addressed by the requirements of ISA 220).
   (c) Whether the four-step approach for embedding quality management principles as presented in revised paragraph 8 of ISA 220 (see **Agenda Item 5-B**) effectively clarifies the overall responsibility for the EP? Is it clear that the overall requirement would be achieved through meeting the requirements in ISA 220, including those that address the core elements and the proposed 'stand-back'?
   (d) The new requirement for the EP to obtain a preliminary understanding of the engagement in order to be able to address the requirements of ISA 220 (see new paragraph 8A in **Agenda Item 5-B**).

D. The Core Elements to be Addressed on All Audits

41. In addition to revising the approach to each core element to incorporate the four-step approach set forth in Section B above, the Task Force has also discussed whether aspects of each core element require restructuring and strengthening (for example, where the respondents to the ITC indicated that a particular aspect should be strengthened or further considered). This section of the Issues Paper sets out the Task Force views on possible changes to ISA 220. Initial thinking on revised drafting for the relevant requirements can be found in **Agenda Item 5-B**).[13]

Information and Communication

42. Although not directly highlighted as part of the responses to the ITC relating to ISA 220 (the issues relating to communication had mainly been presented relating to group audits), communication between the group ET and component auditors was highlighted by many respondents to the ITC as

[13] The revised drafting for each of the below core elements in ISA 220 represents the Task Force's progressed thinking and is subject to further clarification and refinement. However, what is presented in **Agenda Item 5-B** is intended to assist the Board in further understanding the Task Force's proposed approach, including how the four-step approach described in section B above might be applied to each of the core elements.

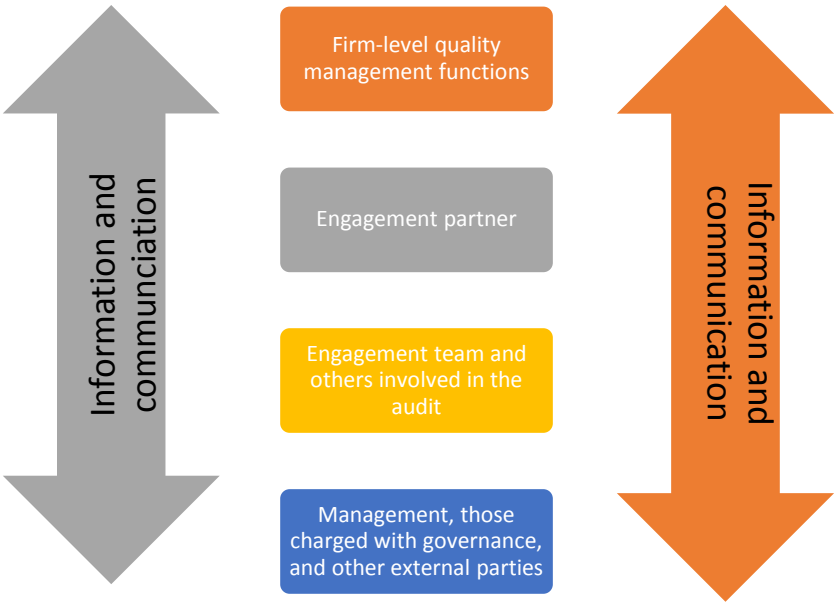
an area where requirements needed to be strengthened. It was noted in the responses related to group audits that two-way communication at all stages of the audit would among other things, enable the group ET to (1) better understand if the instructions provided to the component auditor had been fully understood and that the component auditor was capable of complying with them, and (2) have and improved basis for concluding that sufficient appropriate audit evidence relating to the engagement has been obtained. The Task Force is of the view that this feedback and the related principles are also relevant and should be applied to communications between and among the EP and the ET and any others that might be involved in the audit, as well as between the EP and the firm.

43. In addition, the QCTF has developed new enhanced proposed requirements in ISQC 1related to information and communication for the firm. The proposed draft of ISQC 1 identifies the various information sources and stakeholders with whom two-way communication may take place, including the ET, personnel performing functions in relation to the operation of the firm's system of quality management, firm leadership and parties external to the firm.

44. In light of the increased focus in ISQC 1 on enhanced communication and information, the Task Force's possible enhancements that were discussed by the IAASB in December 2016 included a new proposed requirement for ISA 220 for ongoing, two-way communication among the members of the ET, others involved in the engagement, and the firm and related application guidance (e.g., the EP may communicate resource requirements back to the firm as and when needed or where risks to quality are identified that need to be communicated back to the firm for action at the firm level). The Task Force believes that effective communication among the ET and others involved in the audit sets the foundation for an effective and efficient audit, and helps the EP determine the level of necessary involvement in the audit and the nature, timing and extent of appropriate direction, supervision and review.

45. Board members supported a new requirement in ISA 220 to address communication. However, members cautioned that the proposed new requirement may be overly prescriptive or limiting and may promote a "check-box" mentality. Taking into account the feedback provided by Board members, the Task Force continues to believe that requirement for communication is important, and particularly where the members of the ET are more distributed and involve individuals working in different locations who communicate more on a virtual basis (e.g., where audit delivery models (ADMs) are involved and in situations where the EP is not situated where the majority of the audit work is performed). Further, the Task Force believes that effective communication is the foundation for achieving appropriate direction, supervision and review. Accordingly the Task Force has revised the new proposed requirement to require and promote effective communication among the firm, the EP and the ET (see new paragraph 8B in **Agenda Item 5-B)**.

46. The illustration that follows demonstrates how the Task Force believes the movement of information from the firm down to the ET (and back up) should operate in order to ensure effective communication and ultimately lead to effective management of quality for an audit of financial statements.



47. The Task Force proposes including language in the requirement to clarify that it is the EP's responsibility to communicate information pertaining to quality management at the engagement level that may be relevant to the firm's system of quality management to the appropriate individual(s) within the firm. Likewise, relevant information received about the firm's system of quality management that is relevant to quality management at the engagement level is required to be communicated by the EP to members of the ET or others involved in the audit. These proposed changes also address making such communications on a timely basis. The proposed changes are intended to strengthen the two-way communication relating to matters relating to the firm, such as about the importance, relevance and benefits of the firm's quality management, and about internal and external inspections as relevant (see additional potential application material below).

48. The Task Force also proposes the addition of a requirement that the EP direct the other members of the ET, and others involved in the audit, to communicate information that may be relevant to management of quality at the engagement level to the EP on a timely basis. Consideration will be given to including examples in the application material of the types of communications that this requirement might address.

49. The approach set out above to strengthen the requirements around communication is integral to the Task Force's approach to quality management at the engagement level as described in section C above, and is designed to change behavior at the engagement level.

50. The Task Force will continue to monitor the changes in ISQC 1 (and ISA 600 as relevant) relating to communication to ensure that there is alignment and consistency between the new and revised requirements. For example, the Task Force has currently reflected in its proposed enhancements revisions to the title of this requirement to include "information" to reflect the changes being proposed

in ISQC 1. Conforming wording adjustments will likely be an iterative process as the two projects are progressed.

Application Material

51. As the requirements are further developed, the Task Force is of the view that these could be further supplemented by application material providing examples of appropriate communications in various situations and by describing the different relationships that may exist (specifically within the ET and/or with external parties). The Task Force has progressed its thinking in this regard. For example, the Task Force sees merit in including additional application material that:

- Encourages the communication of appropriate information related to the firm's system of quality management (and communicated by the firm) by the EP to the appropriate members of the ET.
- Encourages communication by the EP about matters relating to the engagement that may be relevant to the firm's system of quality management to the appropriate individuals within the firm responsible for the firm's system of quality management.
- Provides examples of matters that may be communicated from the firm to the ET,[14] such as:
    - Information related to the firm's culture, for example, the message that each individual has a personal responsibility for quality and is expected to comply with the firm's policies or procedures.
    - The firm's responses to quality risks, for example, policies or procedures in relation to the firm's system of quality management that ETs are expected to apply at an engagement level (e.g., the firm's policies or procedures in relation to acceptance and continuance of engagements).
    - Information that describes the authority, roles and responsibilities of personnel performing functions in relation to the engagement.
    - Information related to monitoring and remediation, for example, relevant information about the results of the firm's monitoring and remediation.

  Application guidance could also address the matters that would need to be communicated back to the firm from the ET.
- Includes examples to address timely communication and illustrate interactive communication, as the auditor plans, performs and assesses the work performed, between the EP and ET (and any others involved in the engagement), but in particular for situations where other auditors are used, including ADMs and situations where the EP is not situated where the majority of the audit work is performed.
- Sets out the appropriate types of communications that may be appropriate in different situations, for example in-person, telephonic, in a virtual form, written confirmations, etc.

[14] The bullets below are consistent with ISQC 1 as redrafted, see paragraph A38 of **Agenda Item 2-B**.

- Links back to the documentation requirements in ISA 230[15] regarding communications.

Relevant Ethical Requirements (Including Independence)

52. Although the Task Force did not present proposed enhancements to requirements addressing this core element at the Board's December 2016 meeting, it has continued to consider the impact of introducing the approach to managing quality into the EP's considerations about ethical requirements.

53. The Task Force also discussed the need for revisions to ISA 220 in light of changes arising from revised requirements about the auditor's considerations about non-compliance with laws or regulations (NOCLAR) in both the IESBA Code of Ethics for Professional Accountants (IESBA Code) and ISA 250 (Revised).[16] The Task Force also considered that the QCTF is discussing expanding the relevant ethical requirements in ISQC 1 to other areas (e.g., professional behavior) and that those changes, once discussed with the Board, will need to be reflected in ISA 220 accordingly.

54. The Task Force has currently proposed no changes to the extant requirement in paragraphs 9 and 11, but agrees that additional application material to the requirement would be helpful (see below).

55. However, the Task Force notes that it is not sufficiently clear within paragraph 10 of ISA 220 that the EP may obtain information from other sources (possibly outside of the firm) related to compliance with ethical requirements. Accordingly, the Task Force is of the view that this requirement could be clarified in this regard. (See proposed changes to paragraph 10 in **Agenda Item 5-B**).

Application Material

56. The Task Force is of the view that the relevant ethical requirements could be further supplemented by additional application material to paragraph 9 to emphasize the broader aspects of relevant ethical requirements (i.e., broader than the specific focus in extant ISA 220 and ISQC 1 on independence). This new application material could include examples:

    - Of what could be considered as non-compliance with the ethical requirements, e.g., a failure to identify and address an instance of NOCLAR either by the entity or by the ET.
    - Relating to professional behavior and long association.

    In addition, examples of the EP and ET's considerations when firm-level policies related to ethical requirements are expected to be executed at the engagement level (e.g., on-the-job training and other communications to raise awareness of the importance of compliance with ethical requirements) could also be added.

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[15] ISA 230, *Audit Documentation,* paragraph 8(a) requires "documentation of compliance with the ISAs" and the accompanying application material to this requirement, A7, goes further to explain that "Audit documentation provides evidence that the audit complies with the ISAs. 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:…In relation to 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:… that the engagement partner has taken responsibility for the direction, supervision and performance of the audit in compliance with the ISAs may be evidenced in a number of ways within the audit documentation. This may include documentation of the engagement partner's timely involvement in aspects of the audit, such as participation in the team discussions required by ISA 315 (Revised)."

[16] ISA 250 (Revised), *Consideration of Laws and Regulations in an Audit of Financial Statements*

57. The Task Force discussed adding the following additional application guidance to clarify what is meant by certain phrases within the extant requirement in paragraph 10 including:

- Explaining what is meant by 'other sources' and give examples of what those sources could be. For example, other sources may be in relation to other information that the auditor comes across, other individuals that provide information, etc.
- Describing what is meant by 'appropriate action,' and that it could be one or more of the following:
  - A specific response at the engagement level, which would involve communication within the ET;
  - A specific response at the firm level, which would involve the need for communication with those individuals within the firm responsible for the system of quality management; or
  - A specific response at the network level, which would involve the need to communicate to the network and could involve the need to communicate with external parties.

58. The Task Force is also aware that changes are currently being made to the IESBA Code, and will continue to monitor these changes for any impact on ISA 220.The Task Force also remains mindful that proposed changes to ISA 220 could have implications on the IESBA Code, and therefore continues to consider the possible impact of the proposed changes in ISA 220 on the IESBA Code, if any. The Task Force will coordinate with the IESBA, as relevant, on matters of mutual interest as the revisions to ISA 220 are further developed.

Matters for IAASB Consideration:

6. The IAASB is asked for its views on the new requirement for enhanced information and communication as set out paragraph 8B in **Agenda Item 5-B**, including in light of the changes being proposed in ISQC 1.
7. The IAASB is asked for its views on the matters and possible actions, relating to relevant ethical matters, set out in paragraph 52−58 above.

Acceptance and Continuance of Client Relationships and Audit Engagements

59. The Task Force has proposed changes to the requirements addressing acceptance and continuance of an audit engagement that attempt to introduce the four-step approach for managing quality at the engagement level. Further changes will be necessary to directly align the requirements with the proposed revisions to ISQC 1 in relation to this element once ISQC 1 has been finalized.

60. Neither ISQC 1 nor ISA 220 specify which individuals should be assigned responsibility for making the decision to accept or continue an engagement—the firm's policies or procedures relating to this element would likely specify who should be involved, and may also have graduating levels of required approvals depending on the nature and size of the engagement. In practice these policies or procedures would vary and the designated individual(s) could be a senior leader within the firm or designee, the EP assigned to the engagement, or a combination. If the EP makes the initial conclusion, this may be subject to approval by others within the firm. The Task Force is of the view that the standards need not prescribe who makes the decision to accept or continue the engagement.

Nonetheless, in accepting responsibility for the engagement to which the EP has been assigned, the EP, in considering risks to quality at the engagement level related to this element, should take responsibility for understanding the firm's policies or procedures and how they have been applied in the context of a particular engagement, and determine whether there is anything more that needs to be addressed, or whether there is information that should be communicated to the firm or others. See proposed revisions to paragraph 12 and suggestions for related application guidance set forth in **Agenda Item 5-B**.

61. The Task Force also discussed the requirement in paragraph 13 to communicate information promptly should circumstances arise during the audit that would have caused the firm to decline the audit engagement if that information had been known earlier, and agreed that it was important to maintain this requirement. The Task Force proposes amending this requirement to make it clear that this communication should take place in a timely manner. See proposed revisions to paragraph 13 in **Agenda Item 5-B**.

Matter for IAASB Consideration:

8. The IAASB is asked for its views on the proposed revisions to paragraphs 12 and 13 in **Agenda Item 5-B**. In particular, is it clear what procedures need to be undertaken to comply with this revised requirement? Is there any additional application material that should be considered by the Task Force?

Determination of Engagement Resources, Including Assignment of Engagement Teams

62. Extant ISA 220 sets out the requirements related to the 'assignment of the engagement team.' In revising ISQC 1, the QCTF has considered a broader range of resources that may be required for enhancing the quality of engagements. The QCTF is considering broadening the requirements and application material in relation to the firm's maintenance of sufficient and appropriate resources that are necessary for the proper functioning of the firm's system of quality management and for the performance of engagements. These include financial resources, human resources, technological resources and intellectual resources. The Task Force has agreed that that the corresponding requirements in ISA 220 should also be broadened to require consideration of more than only the assignment of the ET, i.e., to include consideration of a broader range of resources as appropriate at the engagement level, and maintain consistency with the strengthening of ISQC 1. At its December 2016 meeting, the Board supported the following proposed enhancements to this requirement:

- Revise the title of this section to clarify the EP's responsibility for consideration of all resources related to the audit, e.g., ET members (including any other auditors at network firms or ADMs), auditor's experts, automated audit technologies, other data analytics software required, etc.;
- Broaden the requirement by replacing the phrase "engagement team, and any auditor's experts who are not part of the engagement team, collectively have the appropriate competence and capabilities" with "audit engagement has the appropriate and adequate resources necessary to:…" i.e., broadening the EP's responsibilities for ensuring that the assignment of the ET includes all aspects of resources needed for the audit.

63. The Task Force proposes adding a new requirement to ISA 220 (existing paragraph 14 will become part of new paragraph 14A) to introduce the four-step approach for managing quality discussed in Section B above, and to enhance the requirement to include consideration of all resources needed

for the engagement (see new paragraph 14 in **Agenda Item 5-B**). This proposed change will address feedback provided by the Board to broaden the requirement to include all resources (including technology) for the engagement. Application guidance with different examples of the types of resources that could be considered could be developed to support the new and expanded requirement.

64. The Task Force proposes retaining the focus on the competence and capabilities of the members of the ET and any experts who are not part of the ET addressed by extant paragraph 14 in ISA 220. Additionally, controls over the use of technology tools is a relevant and important issue highlighted by the Data Analytics Working Group, as well as by numerous stakeholders. Focusing on these matters was initially discussed with the IAASB at its December 2016 meeting, and based on feedback from the Board, the Task Force added paragraph 14A (see **Agenda Item 5-B**) to reflect the continuing focus on the competence and capabilities of those involved in the audit, and methodologies or technologies (i.e., that they are available and appropriate, including that the ET members have the appropriate skills and experience to use them as intended). The Task Force understands that some tools within the firm are required to be used by all audit ETs, or by certain ETs where the audits have certain attributes, and has proposed the changes within the requirement to reflect this. In these cases, if the firm mandates the use of a particular tool, the firm would be expected to also develop policies or procedures around its use (e.g., in training programs) in order to ensure that audit quality can be achieved on each engagement. The EP has a responsibility to understand firm expectations in respect of the tool, including the objective of the tool, when it should be used, how it works, and if it works, what the expectations are for what needs to be done at the engagement level to support the proper application of the tool (for example, certain engagement specific parameters or inputs may need to be determined by the ET.) Application material would also be developed to provide additional examples of the application of this requirement.

Matter for IAASB Consideration:

9. The IAASB is asked for its views on revised paragraph 14 in **Agenda Item 5-B**. In particular, is it clear what procedures need to be undertaken to comply with this revised requirement? Is there any additional application material that should be considered by the Task Force?

Engagement Performance

Direction, Supervision, Performance and Reviews

65. As discussed in paragraph 15, the Task Force believes that a foundational component of managing quality for an audit engagement is that the EP is sufficiently involved in the engagement in order to have a basis for demonstrating how the objective of ISA 220 has been met. The level of the EP's involvement in the engagement will be a function of the nature, timing and extent of direction, supervision and review, which will therefore be the basis for determining that the EP was indeed "sufficiently involved." This determination will be a matter of professional judgment and will depend on the facts and circumstances of the engagement. The EP's understanding of the entity and its environment, as well as consideration of the other core elements of ISA 220 and how they are being addressed will also help inform the appropriate level of involvement necessary in order to support the conclusion that the EP's involvement was sufficient.

66. In extant ISA 220, the requirements set out that the EP shall take responsibility for the direction, supervision and performance of the engagement,[17] and for the necessary reviews to be undertaken in accordance with firm policies or procedures.[18] At the Board's December 2016 meeting, it was proposed that the requirements that are currently in paragraphs 15 and 16 of ISA 220 be rearticulated and combined into one requirement, supported by the development of additional supporting application material addressing relevant considerations relating to the nature, timing and extent of the EP's involvement in the audit, and by revising the section title to be "Direction, Supervision, Performance, and Reviews." Comments and feedback from the IAASB's discussion at its December 2016 meeting included:

- Overall support for the direction of the proposed revisions to the requirements and application material.
- A suggestion to include considerations that would encourage appropriate application of professional skepticism in the examples in the application material.
- A call for considering more specificity about how direction and supervision should be undertaken, including in situations where the ET is not all in one location.

67. The Task Force is of the view that the performance of the engagement is a collective responsibility of the ET, with the EP taking overall responsibility for the work performed. Performing the work effectively and efficiently therefore involves appropriate direction, supervision and review by the EP but also likely by other members of the ET, or others involved in the audit. The plan for appropriate direction, supervision and review therefore is a function of, and needs to be responsive to, the risks to quality that have been identified when accepting or continuing and planning the engagement. The Task Force is also of the view that the application material to extant paragraph 14 in ISA 220 should highlight that the EP may make assignments to other members of the ET and others involved in the audit, but emphasizing that the EP retains overall responsibility and should have appropriate involvement throughout the engagement in order to be sufficiently involved, i.e., from planning to completion. This will also help explain and link back to new paragraph 3A (see **Agenda Item 5-B**) in the introductory section to the standard.

68. In revising the requirement for the direction, supervision and review of the engagement, the four-step approach for managing quality has been used to embed the quality management principles in this process (see new Paragraph 15A in **Agenda Item 5-B**). The Task Force has also debated how to demonstrate the different responses to risks to quality in the standard, while keeping the requirements principles based, and believes that describing factors that impact the nature, timing and extent of the direction, supervision and review of the engagement will be helpful. Examples of the factors that could be considered include:

- The nature of the entity (including its size and complexity), and the nature of the environment within which it operates;
- The nature of the ET and how it is organized (e.g., whether the ET is located at a single location or at multiple locations, whether an ADM is involved, whether other auditors or component auditors are involved);

[17] ISA 220, paragraph 15

[18] ISA 220, paragraph 16

- The capabilities and competence of the members of the ET and others involved in the audit (i.e., the knowledge, skills and ability of each ET member) including those that have responsibility for direction, supervision and review of other team members;
- The nature, timing and extent of the audit procedures to be performed, e.g., more complex areas may require more hands-on, and more extensive, direction and supervision, and more detailed reviews by more experienced and suitably competent members of the ET; and
- Other relevant factors that may impact the required involvement of the EP.

69. Further, the EP's involvement in the engagement will also be informed by the EP's understanding of the engagement (see proposed new Paragraph 8A in **Agenda Item 5-B**), as well as risks to quality that have been identified and considered in addressing the requirements of ISA 220.

70. Additionally, examples in the application material of differing circumstances will help clarify how to appropriately 'flex' the nature, timing and extent of direction, supervision and review in order to have a basis for concluding that the level of involvement of the EP has been sufficient. For example, different scenarios could be presented, such as:

- An audit of a small, non-complex entity with limited risks—where the nature, timing and extent of active involvement by the EP in the day-to-day oversight of the engagement might be on the lower end of the spectrum (e.g., less frequent interactions with the team as they carry out further audit procedures and higher level reviews of the audit documentation), with relatively more responsibility for direction and supervision of team members being assigned to another suitably experienced and competent member of the ET such as the engagement manager (e.g., daily interactions with team members, on-the-job training and mentoring, and more detailed reviews).
- A new engagement for the firm for an entity that operates in an industry with complex financial reporting issues and the ET is comprised primarily of new staff—where the necessary involvement the EP would need to be on the higher end of the spectrum (e.g., more involvement in the day-to-day oversight of the engagement, including more frequent and more in-person interactions with the team, and more extensive and more detailed reviews being performed by the EP).
- An engagement where some of the audit procedures are undertaken at an ADM—including demonstrating the factors that would need to be taken into account when determining the appropriate nature, timing and extent of the direction, supervision and review when the ET is distributed, i.e., to have a basis for concluding that the involvement of the EP was sufficient.

71. In developing this application material, the Task Force also believes that including specific examples of situations where there are ET members or others involved in the audit who are located in different geographical locations to the EP or when the team operates on a virtual basis (e.g., ADMs, situations where the EP is not located where the majority of the audit work is performed, or where ET members are from network firms or from firms that are not part of the same network) will also help auditors understand how to apply the requirements in different circumstances. The Task Force also notes that these revised requirements will form the foundation for future proposed changes to ISA 600, and will be responsive to calls to further clarify the application of the requirements of ISA 220 to audits of group financial statements.

72. The Task Force also suggests that the application material could build on the concepts in *A Framework for Audit Quality: Key Elements that Create an Environment for Audit Quality*[19] relating to the active involvement of the EP in the planning, supervision and review, as appropriate.

73. With regard to paragraph 17 of extant ISA 220 that addresses reviews of audit documentation by the EP, the Task Force discussed how to emphasize the objective of reviews and how this can be achieved in different circumstances in order to effectively manage the risks to quality at the engagement level. In addition to providing application material of differing circumstances that will help clarify how to appropriately 'flex' the nature, timing and extent of direction, supervision and review described above, in its discussions the Task Force agreed that elevating the application material in paragraph A18 of extant ISA 220 to the requirement in paragraph 17 would help clarify the minimum aspects that the EP is required to review. Paragraph A18 identifies certain areas where the EP should perform timely reviews in order to allow significant matters to be resolved on a timely basis and to the EP's satisfaction. The Task Force believes that additional clarity on where the EP should focus his or her attention would be important and assist the EP in determining whether sufficient appropriate audit evidence has been obtained to support the conclusions reached and the issuance of the auditor's report in the circumstances. The Task Force also has the view that no further prescription is required as the approach to reviews would and should be dependent on the specific circumstances of, and the risks to quality for, each engagement.

74. The Task Force also discussed including additional application material on other suggested areas where the EP may want to focus their reviews, as well as language that encourages the EP to, at a minimum, review the areas required to be reviewed by the EQC reviewer, if there is an EQC reviewer. The Task Force is also of the view that information required to be reviewed by the ECQ reviewer would warrant review by the EP. The Task Force will continue to monitor changes to ISQC 1 to determine the necessary consequential changes to be made in ISA 220, if any, as further consideration is given by the QCTF to EQC reviews.

Matters for IAASB Consideration:

10. The IAASB is asked for its views on the matters set out in paragraphs 65−74 above relating to the direction, supervision, performance and review. Specifically:

    (a) Are the factors describing the impact on the nature, timing and extent of the direction, supervision and review of the engagement described in paragraph 68 helpful? Are there any other factors that would influence the involvement of the EP that should be described?

    (b) Would application material, such as that described in paragraph 70, be sufficient to demonstrate how the nature, timing and extent of the EP's involvement in the audit is 'flexed' based on complexity of the entity and the underlying risks to quality? Are there other examples of different circumstances that should be included?

    (c) Is it clear how addressing the risks to quality described in the standard help the EP determine the nature, timing and extent of the direction, supervision and review that is appropriate for the engagement (i.e., are revised paragraphs 15 and new 15A in **Agenda Item 5-B** sufficiently clear)?

[19] Appendix 2, paragraphs 50–55 of the Framework sets out the key attributes for the EP at the engagement level, including that the EP is actively involved in risk assessment, planning, supervising, and reviewing the work performed.

(d) Should additional application guidance be developed regarding the areas of focus for the EP in undertaking review activities, and if so, what should the areas of focus be?

Consultation and Differences of Opinion

75. These sections include proposed revisions to illustrate how the four-step approach for quality management could be introduced. Additional changes will likely be necessary and will be considered by the Task Force as the QCTF progresses the revisions to these elements in ISQC 1.

76. With regard to the EP's responsibility relating to consultation on difficult and contentious matters, the Task Force is of the view that the relevant aspects of the existing requirement should be retained in the proposed revision to maintain the existing robustness relating to consultation.

EQC Reviews

77. **Agenda Item 2-A** sets out the QCTF's views on a separate standard addressing EQC reviews, which would have a consequential impact on ISA 220 that would need to be considered by the Task Force. Further, it is the view of the Task Force that the EP's responsibilities in relation to the EQC review (as outlined in paragraph 19 of extant ISA 220) should remain in ISA 220 if the requirements relating to the performance of the EQC review are moved to a separate standard. The Task Force will also further consider the EP's responsibilities in light of proposed changes to the criteria for determining when an EQC review is required.

Monitoring

78. The QCTF are proposing that ISQC 1 be strengthened in this area, with the proposed changes including enhanced requirements for monitoring and remediation. The new draft proposed requirement includes, in determining the scope and frequency of the monitoring activities, that the firm take into consideration:

    (a) The design and implementation of the firm's system of quality management;

    (b) Changes in factors that have impacted the firm's system of quality management;

    (c) The results of previous monitoring activities and remedial actions, including whether the previous monitoring activities continue to be relevant in evaluating the firm's system of quality management; and

    (d) Other information that may suggest deficiencies exist in the firm's system of quality management, including information from external inspections, which may indicate the need for the firm to conduct monitoring activities.

79. The ISA 220 Task Force will further consider how the implications of the amendments to monitoring and remediation in ISQC 1 once the IAASB has provided its views on the changes being proposed by the QCTF.

Overall Stand-back before Concluding that Quality has been Effectively Managed at the Engagement Level

80. ISA 220 sets out the core elements required to be addressed in managing quality at the engagement level (see paragraphs 23−26 above). As noted in those paragraphs, the Task Force debated whether

there could be something else other than the core elements that would be relevant to managing quality at the engagement level and that would therefore need to be addressed in ISA 220. As discussed in paragraph 27 within Section C above, the Task Force agreed that these core elements were complete. The Task Force is therefore of the view that appropriate consideration of the requirements of this ISA as they relate to the core elements would provide the basis for the EP's conclusion as to whether quality has been managed effectively at the engagement level, i.e., that the management of quality at the engagement level has been effective in meeting the objective of the standard. The Task Force is, however, also of the view that it would be appropriate for the EP to evaluate, at the end of the engagement, how the requirements of the ISA have been addressed, and in particular whether there are any unaddressed risks to quality (e.g., as a result of new or changed facts and circumstances) that could impact audit quality, and for which additional actions could be necessary.

81. In addition, unexpected changes may arise during the audit that may necessitate the need to develop a response to a "new" risk to quality that may not have been identified through the other discrete requirements within ISA 220 (e.g., acceptance and continuance, determination of engagement resources, etc.). For example, should information come to the attention of the EP during the audit related to poor inspections findings in relation to a component auditor, the EP may need to adjust the approach to directing and supervising the work of that component auditor, including the nature, timing, and frequency of communications and nature and extent of reviews of their work. This risk to audit quality may not have been identified when the EP initially determined and selected the engagement resources, but given that it represents a risk to quality that has now been identified additional actions will need to be undertaken. The Task Force therefore proposes a stand-back requirement to be included in ISA 220 (see new paragraph 23A in **Agenda Item 5-B**).

82. This stand-back approach is consistent with the approach taken in other ISAs that seeks to achieve a quality audit. For example, paragraph 25 of ISA 330, in the section on "Evaluating the Sufficiency and Appropriateness of Audit Evidence," states that "Based on the audit procedures performed and the audit evidence obtained, the auditor shall evaluate before the conclusion of the audit whether the assessments of the risks of material misstatement at the assertion level remain appropriate." The Task Force also believes that including such a stand-back requirement would also assist in supporting the exercise of professional skepticism by the EP and other members of the ET.

83. The Task Force believes that this stand-back concept would be best applied in ISA 220 by requiring the EP to consider, before the completion of the audit and prior to forming a conclusion on the financial statements, whether the risks to quality have been appropriately addressed. The Task Force proposes that the requirement be supported by application material to explain that although this requirement is performed at the end of the engagement, it is not meant to preclude the EP from taking actions throughout the course of the engagement should other risks to quality arise while performing each of the discrete requirements in this standard. The Task Force also notes that a conforming amendment to ISA 700 (Revised),[20] paragraph 11 might be appropriate, i.e., to include consideration of "the engagement partner's conclusion that quality has been effectively managed at the engagement level (ISA 220)" as part of the overall stand-back before forming an opinion on the financial statements.

[20] ISA 700 (Revised), *Forming an Opinion and Reporting on Financial Statements*

Matter for IAASB Consideration:

11. The IAASB is asked for its views on the matters set out in paragraphs 80−83 above relating to a new requirement for an overall stand-back before concluding that quality has been effectively managed and achieved at the engagement level.

Other Elements of ISA 220

Definitions

84. No changes were presented for the December 2016 IAASB meeting to any of the definitions within ISA 220. At the IAASB meeting, Board members highlighted that these definitions were consistent with the same definitions in the IESBA Code. The Board therefore noted that caution should be exercised in considering changes, and that collaboration with the IESBA would be important if any changes were believed to be necessary.

85. However, as it relates to the definition of EQC reviewer, the QCTF is currently considering changes to the definition as well as changes relating to the role and responsibilities of the EQC Reviewer – any changes, if any, made to the definition in ISQC 1 will therefore need to be replicated in ISA 220 once finalized.

86. In addition, QCTF is considering a new definition of "Quality Risk". If supported by the Board, this definition would likely need to also be included within ISA 220, potentially amended for specific application in the context of an audit engagement. The QCTF's discussion of the proposed definition in **Agenda Item 2-A** notes the need for the definition to be further considered in conjunction with the ISA 220 Task Force as it is also relevant to the concepts in ISA 220. The proposed definition included within **Agenda Item 2-B** is as follows:

> Quality Risk – A risk that, individually or in combination, could reasonably have an adverse impact on the firm's ability to achieve its quality objectives.

87. Although the Task Force proposes no further revisions to any definitions in ISA 220 at this stage; however this may change based on further discussions of the QCTF and the Task Force and Board input. If changes to the definitions are ultimately contemplated, the Task Force acknowledges that any changes will need to be made in careful coordination with the IESBA. Consistent with Board feedback, the Task Force also continues to have the view that additional application material supporting the definitions as described in Agenda Item 8-B of the December 2016 IAASB meeting agenda materials (and as set out below) will be helpful in illustrating how the definitions might be applied to different and evolving situations.

Application Material

88. In relation to the definitions, the following application material could be considered (either to the definitions or in support of specific requirements in the standard):

    (a) Engagement team – Providing examples of different types of ETs, including examples of individuals who would form part of the ET, including:

        - Individuals working on the engagement who are situated at or part of ADMs – through describing various scenarios of such arrangements as well as demonstrating the considerations for ETs to apply in determining whether to use an ADM and how use of

an ADM should be addressed in designing appropriate direction, supervision and review (see paragraph 94 below).

- Individuals from a network firm that are involved in the audit, but who do not meet the definition of component auditors in ISA 600 (including addressing the impact on the direction, supervision and review by the EP).
- Other examples where individuals may be working on an engagement that is not a traditional structure (i.e., not all working from the same location, engaged from other firms not included in the network).

(b) EQC Reviewer – Clarify that the EQC reviewer is not considered a member of the ET and that the work of the EQC reviewer is not considered audit procedures.

(c) **Agenda Item 4-A** sets out the discussion regarding networks. At this stage it is not contemplated that there will need to be a change to the definition but discussions of that paper may highlight the need for additional application material (either in ISA 220 or in ISQC 1, or possibly both) to highlight the different types of network arrangements that exist, and how network-level policies or procedures may be relevant to, and should be considered as part of managing quality at the firm and engagement level.

Additional Topics Discussed by the Task Force

ADMs

89. Within ISA 220 specifically, the topic of ADMs has become more relevant because of the growing use of centralized resources by ETs and the various ways that firm and ET structures are evolving. ADMs may be designed or intended to enhance audit quality, but may also give rise to new or different risks to quality at the engagement level. In particular, considerations related to ADMs are important for requirements addressing information and communication, determination of engagement resources, and direction, supervision, and review. This section of the Issues paper addresses matters related to ADMs that have been discussed by the Task Force. Certain matters are also addressed in the proposals for additional application guidance in the rest of this paper and in the proposed revisions to ISA 220 included in **Agenda Item 5-B**.

90. The ITC used the phrase “ADMs” to cover terms such as “firm shared service centers,” “centers of excellence,” “on-shoring,” “offshoring,” or “outsourcing”—essentially capturing how firms are reorganizing their structures and ETs, often in order to perform high quality audits at a reasonable cost. Respondents to the ITC supported actions to address issues around ADMs and other similar situations where other auditors are used. In considering the most appropriate actions, the Task Force agreed that additional application material is needed to help clarify that the definition of ET incorporates all those individuals who are under the direction, supervision and review of the EP (with the exception of those specifically covered by other ISAs as noted).

91. To help demonstrate who is considered to be part of the ET, examples of various scenarios could be provided as application material to the definition of ET to illustrate where other auditors, who are not in the same place as the ET, form part of the ET. The Task Force is of the view that this approach would help auditors to distinguish who is part of the ET without specifically defining the concept “ADM,” which would be difficult due to the wide-ranging circumstances to which the term may apply.

92. To that end, the Task Force discussed several examples of how other auditors at ADMs are currently being used by ETs including:

    (a) At the planning stage, procedures to set up current year work papers, such as roll forward of prior year schedules, set up of analytics, trial balance and population of lead schedules and summaries of various reports and minutes;

    (b) Substantive procedures that are "objective based" in areas such as cash (confirmations), inventory, accounts payable, accounts receivable, revenue, debt and plant property and equipment. Such substantive procedures could include testing the mathematical accuracy of a population, recalculations, checking reconciliations, verifying data in a population and external confirmation and data requests;

    (c) At the completion stage, procedures could include financial statement tie out, preparation of cash flows, performing disclosure checklists; and

    (d) Other areas included providing assistance with testing information technology general controls, journal entry testing, review of service organization reports to identify follow-up items, and quality checklists.

93. The Task Force believes that including examples in the application material describing the activities of individuals involved in the engagement at ADM's may help clarify that these individuals are part of the ET, and therefore that the responsibilities of the ET members also applies to these individuals (i.e., separate requirements addressing individuals at ADMs is not needed). Such examples could also incorporate who/what is considered to be an ADM—signaling to ETs that a broad range of scenarios may be included in the definition of ET:

    - Audit-related activities are outsourced to individuals that are not located within the local ET's jurisdiction;
    - Audit-related activities are outsourced to individuals that are located within the same jurisdiction, but not in the same location, as the local ET; and
    - Audit-related activities are outsourced to individuals not under the auditing firm's system of quality management (i.e., a third party).

94. Notwithstanding individuals situated at ADMs are part of the ET, there are also special considerations about the appropriate level of direction and supervision of the individuals at the ADMs, and review of the procedures performed when ADM arrangements exist. The Task Force is of the view that developing application material to illustrate what these considerations could be may also help embed the quality management principles by illustrating the 'flexing' of what needs to be done based on the circumstances. Identifying characteristics that would impact the auditor's assessment of the timing, nature and extent of direction, supervision and review would also allow changing circumstances to be addressed as these arrangements continue to evolve. Relevant considerations that would impact the nature, timing and extent of the EP's direction, supervision and review could include:

    (a) Risk, complexity and level of judgment required to perform the procedure(s) performed at the ADM;

    (b) Restrictions arising from laws and regulations (e.g., confidentiality);

(c) Applicable firm policies or procedures for quality management that are relevant to the ADM or centralized location;

(d) Previous experience with the ADM or centralized location, as well as consideration of the results of any monitoring and remediation activities relating to that location; and

(e) Competence of the individuals at the ADM.

These characteristics could be presented in the application material to help the EP determine the timing, nature and extent of their direction, supervision and review. The examples could also be developed to show the impact of different circumstances.

E. Way Forward

95. The Task Force will continue to develop the changes to ISA 220 based on feedback from the Board, and other planned outreach in the second half of 2017, with the objective of being able to present a first read of an exposure draft to the IAASB in December 2017. The Task Force will also continue to monitor the changes being made to ISQC 1 to ensure consistency of the changes being made in ISA 220 where appropriate.

96. The Task Force also continues to consider issues around experts or individuals with specialized skills who are considered part of the ET, and whether external experts engaged by the auditor should be part of the ET. These matters will be further discussed by the Task Force and recommendations, if any, discussed with the Board at a future Board meeting.

Matter for IAASB Consideration:

12. Are there any other matters that the Task Force should consider in progressing the revision to ISA 220?

Appendix A

Approved Minutes – December 2016 IAASB Meeting

Quality Control – ISA 220

Ms. Zietsman presented the Board with the Crossover Working Group's (Crossover WG's) initial views on possible revisions to ISA 220 from the responses to the ITC as set out in **Agenda Items 8-A and 8-B**. The possible revisions included suggested enhancements to many of the extant requirements and application guidance in ISA 220, the introduction of possible new requirements to embed quality management principles at the engagement level and to address communications among members of the engagement team and others involved in the audit.

There was general agreement from the Board on the direction of the proposed enhancements put forward by the Crossover WG, with some areas for further consideration by the Task Force noted variously by Board members, including:

- Although supporting linking the objective of the auditor to managing quality of the audit, it was noted that more clarity about how this would be operationalized in ISA 220 is required (in particular the interaction between a risk assessment for these purposes (i.e. risks to quality) versus the assessment of the risks of material misstatement as required by ISA 315 (Revised));
- Support for clarifying the engagement partner's (EP) overall responsibility and accountability for audit quality at the engagement level, while still allowing the EP the flexibility to assign certain responsibilities to other members of the engagement team;
- Further consideration of situations where the signing partner is different from the EP who was responsible for the direction supervision, and review of the work performed as a part of the audit;
- The need for appropriate coordination with the IESBA relating to considerations around the definitions of EP, engagement team, and network firms;
- Support for a new requirement related to strengthening two-way communication among the members of the engagement team and those involved in the audit; and
- Support for further consideration of how firms in networks interact, especially as relates to quality control

PIOB OBSERVER REMARKS

Prof. Van Hulle encouraged the Task Force to further consider supervision of auditors where audit work has been outsourced (e.g., to other auditors), in particular as it relates to responsibilities for direction, supervision and review as well as communication.

WAY FORWARD

The Crossover WG will continue to progress possible changes to ISA 220 for discussion by the IAASB at future meetings, including further considering how to embed quality management principles at the engagement level.

Working Draft of Proposed Amendments to ISA 220 Requirements

(Note: The proposed revisions presented below represent the ISA 220 Task Force's views that have been progressed since the December 2016 IAASB meeting. The proposed enhancements to the requirements will be subject to further changes as the ISA 220 Task Force continues to deliberate matters related to ISA 220, in particular as it relates to the Task Forces proposed 'four-step approach' described in paragraph 31 of Agenda Item 5-A, as well as revisions being made to ISQC 1)

ISA 220 Para ref.	ISA 220 Current Requirements	Proposed Enhancements to Requirements	Matters for Further Consideration / Reference to Relevant Paragraph in the Issues Paper (Agenda Item 5-A)
Introduction			
Scope			
1	This International Standard on Auditing (ISA) deals with the specific responsibilities of the auditor regarding quality control procedures for an audit of financial statements. It also addresses, where applicable, the responsibilities of the engagement quality control reviewer. This ISA is to be read in conjunction with relevant ethical requirements.	This International Standard on Auditing (ISA) deals with the specific responsibilities of the auditor regarding management of quality ~~control procedures~~ for an audit of financial statements. [It also addresses, where applicable, the responsibilities of the engagement quality control reviewer.][1] This ISA is to be read in conjunction with relevant ethical requirements.	*Refer to paragraphs 11–16 within Issues Paper*
~~System of~~ Quality ~~Control~~ Management at the Firm and Engagement Level, ~~and~~ the Role of Engagement Teams and Interaction with other International Standards			
2	Quality control systems, policies and procedures are the responsibility of the audit firm. Under ISQC 1,[2] the firm has an obligation to establish and maintain a system of quality	Quality ~~control systems, policies and procedures are~~ management is the responsibility of the audit firm. Under ISQC	*Refer to paragraphs 11–16 within Issues Paper*

[1] Agenda Item 2–A, paragraphs 123-133, notes that the ISQC 1 Task Force (QCTF) is of the view that it would be beneficial at this time to determine whether or not the requirements relating to the EQC review should be incorporated into a separate standard. The ISA 220 Task Force will make changes to ISA 220 as appropriate once the Board views on this matter have been obtained.

[2] International Standards on Quality Control (ISQC) 1, *Quality Control for Firms that Perform Audits and Reviews of Financial Statements, and Other Assurance and Related Services Engagements*

ISA 220 Para ref.	ISA 220 Current Requirements	Proposed Enhancements to Requirements	Matters for Further Consideration / Reference to Relevant Paragraph in the Issues Paper (Agenda Item 5-A)
	control to provide it with reasonable assurance that: (a) The firm and its personnel comply with professional standards and applicable legal and regulatory requirements; and (b) Reports issued by the firm or engagement partners are appropriate in the circumstances. This ISA is premised on the basis that the firm is subject to ISQC 1 or to national requirements that are at least as demanding. (Ref: Para. A1)	1[3], the firm has an obligation to establish and maintain ~~a~~ its system of quality ~~control~~ management to provide it with reasonable assurance that: (a) The firm and its personnel comply with professional standards and applicable legal and regulatory requirements; and (b) Reports issued by the firm or engagement partners are appropriate in the circumstances.[4] This ISA addresses the application of quality management at the engagement level within the context of the firm's system of quality management for an audit of financial statements. This ISA is premised on the basis that the firm is subject to ISQC 1 or to national requirements that are at least as demanding. (Ref: Para. A1)	Further consideration to also be given to necessary changes to the application guidance in A1 to address the revision of ISQC 1 to incorporate a quality management approach.
		2A.[NEW] Quality management at the firm-level addresses all engagements that the firm performs (including audits and reviews of financial statements, and other assurance and related services engagements) and encompasses a quality management process	*Refer to paragraphs 11–16 within Issues Paper* Application guidance to be considered to further explain how quality management at the engagement level builds on and includes executing on responses

[3] ISQC 1, *Quality Control for Firms that Perform Audits and Reviews of Financial Statements and Other Assurance and Related Services Engagements*

[4] ~~International Standards on Quality Control~~ (ISQC) 1, ~~*Quality Control for Firms that Perform Audits and Reviews of Financial Statements, and Other Assurance and Related Services Engagements*~~, paragraph 11

ISA 220 Para ref.	ISA 220 Current Requirements	Proposed Enhancements to Requirements	Matters for Further Consideration / Reference to Relevant Paragraph in the Issues Paper (Agenda Item 5-A)
		that involves establishment of quality objectives, performance of quality risk assessment, design and implementation of responses to address quality risks and monitoring and remediation. Quality management for an audit of financial statements is integrated with and addressed in the context of the firm's system of quality management and includes executing on responses that are required to be performed at the engagement level and also determining additional responses necessary for the specific engagement.	established at the firm level by the firm's system of quality management which addresses the requirements of ISQC 1.
		2B. [NEW] Quality management at the firm level requires that the firm obtain or generate, and communicate relevant information necessary to enable and support the proper functioning of the firm's system of quality management. This includes establishing policies and procedures to facilitate the communication of the relevant information with relevant parties that enables the firm and relevant parties to take appropriate and timely action in relation to such information.	*Refer to paragraphs 11–16 within Issues Paper* Application guidance to be added to refer to the relevant requirements of ISQC 1 (i.e., that address information and communication).
3	Within the context of the firm's system of quality control, engagement teams have a responsibility to implement quality control procedures that are applicable to the audit	3. ~~Within the context of the firm's system of quality control, engagement teams have a responsibility to implement quality control procedures that are applicable to the audit~~	*Refer to paragraphs 11– 16 within Issues Paper* Application guidance to be added that explains what the "core elements" are in

ISA 220 Para ref.	ISA 220 Current Requirements	Proposed Enhancements to Requirements	Matters for Further Consideration / Reference to Relevant Paragraph in the Issues Paper (Agenda Item 5-A)
	engagement and provide the firm with relevant information to enable the functioning of that part of the firm's system of quality control relating to independence.	~~engagement and provide the firm with relevant information to enable the functioning of that part of the firm's system of quality control relating to independence.~~ For an audit of financial statements, the engagement partner has responsibility for managing quality at the engagement level within the context of the firm's system of quality management. The requirements of this ISA address managing quality for an audit of financial statements. In addressing the requirements of this ISA, the engagement partner has responsibility for: • Implementing actions or procedures designed or established at the firm-level to address quality risks that are applicable to the audit engagement • Communicating relevant information to the firm to enable the effective functioning of the firm's system of quality management.	this context. e.g., aspects of quality control that are required to be addressed in an audit including: • Relevant Ethical Requirements, • Acceptance and Continuance of Client Relationships and Audit Engagements. • Assignment of Engagement Teams. • Engagement Performance (including direction, supervision and performance; reviews; consultation; engagement quality control review and differences of opinion). • Monitoring.
		3A [NEW] Although the engagement partner has responsibility for managing quality at the engagement level for an audit of financial statements, it is not expected, and in many cases not practical, that all of the requirements of this ISA are addressed solely by actions, tasks or procedures performed by the engagement partner. The engagement	*Refer to paragraph 15 within Issues Paper* Consideration to be given to highlight activities that are likely not appropriate for the EP to assign. Also to highlight situations that might result in the EP not being sufficiently involved in order to

ISA 220 Para ref.	ISA 220 Current Requirements	Proposed Enhancements to Requirements	Matters for Further Consideration / Reference to Relevant Paragraph in the Issues Paper (Agenda Item 5-A)
		partner may therefore assign actions, tasks or procedures to others to assist the engagement partner. However, regardless of who performs required actions, tasks or procedures, the engagement partner remains responsible overall for determining that the requirements are appropriately addressed. The engagement partner is therefore responsible for being sufficiently involved in the engagement in order to have an appropriate basis for demonstrating how the requirements of this ISA have been addressed. In some cases, the ISAs or firms may specify that certain actions, tasks or procedures be performed by the engagement partner personally; accordingly, the assignment of such actions, tasks or other procedures to other members of the engagement team would not be appropriate.	have a basis for taking responsibility for managing quality at the engagement level (including for example, audits of letterbox companies where the EP is not sufficiently involved in the direction, supervision and performance of the engagement). See also changes to paragraphs 15 and 16 below.
		3B [NEW] Information obtained from addressing requirements of other ISAs will also be relevant to managing quality at the engagement level. In addition to the information used as the basis for the decision to accept or continue the engagement in accordance with the firm's policies and procedures, certain other information will be available to the engagement partner and	*Refer to paragraphs 17–18 within Issues Paper* • Additional application material to highlight and explain the need for interaction of the engagement level quality management policies and procedures with other activities at the engagement level, including those performed at the beginning of

ISA 220 Para ref.	ISA 220 Current Requirements	Proposed Enhancements to Requirements	Matters for Further Consideration / Reference to Relevant Paragraph in the Issues Paper (Agenda Item 5-A)
		engagement team at the beginning of the audit engagement and as the planning and risk assessment activities commence. For example: • ISA 210,[5] which deals with the auditor's responsibilities in agreeing the terms of an audit engagement. • ISA 315 (Revised),[6] which deals with the auditor's responsibility to identify and assess the risks of material misstatement in the financial statements through understanding the entity and its environment, including the entity's internal control. All relevant information available to the engagement partner and engagement team may therefore assist in designing the planned responses to address the requirements of this ISA.	the engagement (client acceptance/continuance, ISA 210, ISA 315 (Revised)), the design of the audit plan (ISA 300) and also highlighting the need to consider additional information learned as the audit progresses (recognizing that the performance of an audit is not linear and that many activities are inter-related). • Additional application material to be considered to provide further examples of the types of information that may be relevant to more than one standard.
		3C [NEW] Information obtained from addressing the requirements of this ISA may also be relevant when dealing with the requirements of ISA 300 that relate to	*Refer to paragraphs 17–18 within Issues Paper* Application guidance to be developed that will reference paragraphs 2, 6 and 13 of ISA 300[7] which describe aspects

[5] ISA 210, *Agreeing the Terms of Audit Engagements*

[6] ISA 315 (Revised), Identifying and Assessing the Risks of Material Misstatement through Understanding the Entity and Its Environment

[7] ISA 300, *Planning an Audit of Financial Statements*

ISA 220 Para ref.	ISA 220 Current Requirements	Proposed Enhancements to Requirements	Matters for Further Consideration / Reference to Relevant Paragraph in the Issues Paper (Agenda Item 5-A)
		establishing the overall audit strategy for the engagement and developing the audit plan.	of quality management that impact planning the audit (including when considering the role and timing of planning, and preliminary engagement activities). Additional consideration to also be given to the need for any conforming amendments to ISA 300.
		3D [NEW] In addressing the requirements of ISA 315 (Revised), the auditor is required to revise the assessment of the risks of material misstatement and modify further planned audit procedures accordingly if new information is obtained, or audit evidence from performing further audit procedures is inconsistent with audit evidence on which the auditor originally based the assessment.[8] Such information or audit evidence may also be relevant to managing quality at the engagement level, and accordingly, it may be necessary for the engagement partner to modify planned responses or implement new responses to address the requirements of this ISA. Similarly, the engagement partner may need to communicate relevant information to the members of the engagement team or the	*Refer to paragraphs 17–18 within Issues Paper* Further consideration to be given to application guidance with more specific references to ISA 315 (Revised), including the requirement to revise risk assessment as new audit evidence is obtained (paragraph 31), and examples of how these revisions might affect quality management at the engagement level. In addition, additional application guidance to be considered to provide further examples of the types of information that may be relevant to more

[8] ISA 315 (Revised), paragraph 31, states that the auditor's assessment of the risks of material misstatement at the assertion level may change during the course of the audit as additional audit evidence is obtained. In circumstances where the auditor obtains audit evidence from performing further audit procedures, or if new information is obtained, either of which is inconsistent with the audit evidence on which the auditor originally based the assessment, the auditor shall revise the assessment and modify the further planned audit procedures accordingly. (Ref: Para. A152).

ISA 220 Para ref.	ISA 220 Current Requirements	Proposed Enhancements to Requirements	Matters for Further Consideration / Reference to Relevant Paragraph in the Issues Paper (Agenda Item 5-A)
		firm (in the context of supporting the effective functioning of the firm's system of quality management.)	than one standard, and how it should be addressed by the auditor.
4	Engagement teams are entitled to rely on the firm's system of quality control, unless information provided by the firm or other parties suggests otherwise. (Ref: Para. A2)	TBD	Consideration of firm and network-level policies and procedures at the engagement level is addressed separately in **Agenda Item 4-A**. Changes to paragraph 4 of extant ISA 220 and related application guidance will be considered by the Task Force based on the outcome of the IAASB's discussion.
Effective Date			
5	This ISA is effective for audits of financial statements for periods beginning on or after December 15, 2009.	TBD	N/A
Objective			
6	The objective of the auditor is to implement quality control procedures at the engagement level that provide the auditor with reasonable assurance that: (a) The audit complies with professional standards and applicable legal and regulatory requirements; and (b) The auditor's report issued is appropriate in the circumstances.	The objective of the auditor is to ~~implement quality control procedures~~ manage and achieve quality at the engagement level ~~that~~ in order to provide the auditor with reasonable assurance that: (a) The audit complies with professional standards and applicable legal and regulatory requirements; and	*Refer to paragraph 20 within Issues Paper*

ISA 220 Para ref.	ISA 220 Current Requirements	Proposed Enhancements to Requirements	Matters for Further Consideration / Reference to Relevant Paragraph in the Issues Paper (Agenda Item 5-A)
		(b) The auditor's report issued is appropriate in the circumstances.	
Definitions			
7	For purposes of the ISAs, the following terms have the meanings attributed below: (a) Engagement partner[9] – The partner or other person in 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 required, has the appropriate authority from a professional, legal or regulatory body. (b) Engagement quality control review – A process designed to provide an objective evaluation, on or before the date of the auditor's report, of the significant judgments the engagement team made and the conclusions it reached in formulating the auditor's report. The engagement quality control review process is for audits of financial statements of listed entities and those other audit engagements, if any, for which		*Refer to paragraphs 84−88 within Issues Paper*

[9] "Engagement partner," "partner," and "firm" should be read as referring to their public sector equivalents where relevant.

ISA 220 Para ref.	ISA 220 Current Requirements	Proposed Enhancements to Requirements	Matters for Further Consideration / Reference to Relevant Paragraph in the Issues Paper (Agenda Item 5-A)
	the firm has determined an engagement quality control review is required. (c) Engagement quality control reviewer – A partner, other person in the firm, suitably qualified external person, or a team made up of such individuals, none of whom is part of the engagement team, with sufficient and appropriate experience and authority to objectively evaluate the significant judgments the engagement team made and the conclusions it reached in formulating the auditor's report. (d) Engagement team – All partners and staff performing the engagement, and any individuals engaged by the firm or a network firm who perform audit procedures on the engagement. This excludes an auditor's external expert engaged by the firm or a network firm.[10] The term "engagement team" also excludes individuals within the client's internal audit function who provide direct assistance on an audit engagement when the external auditor complies with the		

[10] ISA 620, *Using the Work of an Auditor's Expert*, paragraph 6(a), defines the term "auditor's expert."

ISA 220 Para ref.	ISA 220 Current Requirements	Proposed Enhancements to Requirements	Matters for Further Consideration / Reference to Relevant Paragraph in the Issues Paper (Agenda Item 5-A)
	requirements of ISA 610 (Revised 2013)[11]. (e) Firm – A sole practitioner, partnership or corporation or other entity of professional accountants. (f) Inspection – In relation to completed audit engagements, procedures designed to provide evidence of compliance by engagement teams with the firm's quality control policies and procedures. (g) 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. (h) Monitoring – A process comprising an ongoing consideration and evaluation of the firm's system of quality control, including a periodic inspection of a selection of completed engagements, designed to provide the firm with reasonable assurance that its system of quality control is operating effectively.		

[11] ISA 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.

ISA 220 Para ref.	ISA 220 Current Requirements	Proposed Enhancements to Requirements	Matters for Further Consideration / Reference to Relevant Paragraph in the Issues Paper (Agenda Item 5-A)
	(i) Network Firm – A firm or entity that belongs to a network. (j) Network – A larger structure: 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 control policies and procedures, common business strategy, the use of a common brand name, or a significant part of professional resources. (k) Partner – Any individual with authority to bind the firm with respect to the performance of a professional services engagement. (l) Personnel – Partners and staff. (m) Professional standards – International Standards on Auditing (ISAs) and relevant ethical requirements. (n) Relevant ethical requirements – Ethical requirements to which the engagement team and engagement quality control reviewer are subject, which ordinarily comprise Parts A and B of the International Ethics Standards Board for Accountants' *Code of Ethics for*		

ISA 220 Para ref.	ISA 220 Current Requirements	Proposed Enhancements to Requirements	Matters for Further Consideration / Reference to Relevant Paragraph in the Issues Paper (Agenda Item 5-A)
	Professional Accountants (IESBA Code) related to an audit of financial statements together with national requirements that are more restrictive. (o) Staff – Professionals, other than partners, including any experts the firm employs. (p) Suitably qualified external person – An individual outside the firm with the competence and capabilities to act as an engagement partner, for example, a partner of another firm, or an employee (with appropriate experience) of either a professional accountancy body whose members may perform audits of historical financial information or of an organization that provides relevant quality control services.		
Requirements			
Leadership Responsibilities for Quality on Audits			
8	The engagement partner shall take responsibility for the overall quality on each audit engagement to which that partner is assigned. (Ref: Para. A3)	8. The engagement partner shall take responsibility for ~~the overall~~ managing and achieving quality on each audit engagement to which that partner is assigned. In doing so, through addressing the requirements of this ISA, the engagement partner shall:	*Refer to paragraphs 37–40 within Issues Paper* Application Material to be developed to: • Emphasize that the engagement partner needs to have an understanding of the entity and its

ISA 220 Para ref.	ISA 220 Current Requirements	Proposed Enhancements to Requirements	Matters for Further Consideration / Reference to Relevant Paragraph in the Issues Paper (Agenda Item 5-A)
		(a) Understand the firm's policies or procedures that are relevant to the engagement; (b) Determine whether such policies or procedures are sufficient and effective, and whether other actions are necessary; (c) Identify actions to respond to risks to quality for the engagement; and (d) Communicate matters related to quality with the firm, engagement team or others as appropriate	environment to be able to address responsibilities for managing quality for the engagement (cross references to ISA 315 (Revised)). • Remind auditors about the importance of information and communication between the engagement partner and the: o Firm relevant to the firm's system of quality management. o Engagement team in order that the engagement team has the information necessary to perform the audit. • Revise the extant application material in A3 to explicitly state that the engagement partner's actions include appropriate messaging to the engagement team to "emphasize all members of the engagement team have a responsibility to deliver a quality audit," i.e., emphasize "tone at the top" • Emphasize the importance of appropriate involvement by the engagement partner at all stages of the audit (planning, performance, completion).

ISA 220 Para ref.	ISA 220 Current Requirements	Proposed Enhancements to Requirements	Matters for Further Consideration / Reference to Relevant Paragraph in the Issues Paper (Agenda Item 5-A)
			• Explain what is meant by policies or procedures 'operating effectively.'
		8A. [NEW] In order to have the appropriate basis for planning and implementing the approach to managing quality at the engagement level, the engagement partner shall obtain a preliminary understanding of the nature and circumstances of the engagement.	To support the new requirement in proposed paragraph 8A, new application material to explain the types of matters the EP would need to understand to be able to apply the requirements in this standard, for example: • The nature of the entity (e.g., whether it is a business enterprise, a public sector entity or a not-for-profit organization) and the industry in which it operates (some industry's require expertise); • The relevant applicable financial reporting framework; • Organization and structure; and • Laws and regulations. In addition, the application guidance would need to explain that the understanding referred to in paragraph 8A forms the basis for applying the 4-step approach (set out in paragraph 8 above) to the requirements of this ISA.

ISA 220 Para ref.	ISA 220 Current Requirements	Proposed Enhancements to Requirements	Matters for Further Consideration / Reference to Relevant Paragraph in the Issues Paper (Agenda Item 5-A)
Information and Communication			
8B [NEW]	***NOT EXTANT – This is what was presented at the Dec 2016 Board Meeting; Extant ISA 220 has no requirements that explicitly address communication*** NEW requirement: In addition to the specific communication requirements of the ISAs, when performing audit procedures to comply with the ISAs the engagement partner and engagement team (and any others involved in the engagement) shall have ongoing, frequent and comprehensive two-way communication.	8B [NEW] In addition to the specific requirements for communication, including the information that shall be communicated in the ISAs (including this ISA) and ISQC 1, the engagement partner shall, on a timely basis, communicate relevant information pertaining to quality management at the engagement level to: (a) Members of the engagement team or others involved in the audit; and (b) As necessary or as appropriate, to members of management of the firm for whom the information is relevant, including as appropriate, the firm, personnel performing functions in relation to the firm's system of quality management, or, parties external to the firm. The engagement partner shall also direct the other members of the engagement team and any others involved in the audit to communicate information that may be relevant to management of quality at the engagement level to the engagement partner on a timely basis.	*Refer to paragraphs 42–51 within Issues Paper* Additional application guidance to be considered to: • Address what 'on a timely basis' means – including that it will depend on the circumstances of the engagement, but also on the nature of the matter being communicated. • Explain that the firm may require communication of certain information by the engagement partner; however in some cases, it may be necessary or appropriate for the engagement partner to make communications to appropriate firm management. • Address when communications to external parties may be expected or appropriate. • Provides examples of "relevant information" pertaining to quality management that may be communicated from the firm to the engagement team and the types of

ISA 220 Para ref.	ISA 220 Current Requirements	Proposed Enhancements to Requirements	Matters for Further Consideration / Reference to Relevant Paragraph in the Issues Paper (Agenda Item 5-A)
			things that would need to be communicated back to the firm from the engagement team (building off the examples provided in ISQC 1). Similarly – add examples of what might be relevant matters for engagement team members to communication to the EP on a timely basis
Relevant Ethical Requirements			
9	Throughout the audit engagement, the engagement partner shall remain alert, through observation and making inquiries as necessary, for evidence of non-compliance with relevant ethical requirements by members of the engagement team. (Ref: Para. A4–A5)	Discussions and proposed changes still under consideration by the Task Force	*Refer to paragraphs 52–58 within Issues Paper* *Further changes to be considered as necessary arising from revisions to ISQC 1.*
10	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, the engagement partner, in consultation with others in the firm, shall determine the appropriate action. (Ref: Para. A5)	If matters come to the engagement partner's attention through the firm's system of quality ~~control~~ management, through the requirement in paragraph 9, or from other sources ~~or otherwise~~ that indicate that members of the engagement team have not complied with relevant ethical requirements, the engagement partner, in consultation with others in the firm, shall determine the appropriate action. (Ref: Para. A5)	*Refer to paragraphs 52–58 within Issues Paper* Task Force considering need for changes and additional application guidance, taking account of revisions to ISQC 1, and including: • Additional guidance on where relevant information may come from (the output of the firm's systems,

ISA 220 Para ref.	ISA 220 Current Requirements	Proposed Enhancements to Requirements	Matters for Further Consideration / Reference to Relevant Paragraph in the Issues Paper (Agenda Item 5-A)
			from members of the engagement team, from external sources) • Additional guidance to address who the others might be that the engagement partner would consult with and what "appropriate action" might entail at the engagement level, including communications within the engagement team, to management and those charged with governance of the audited entity, to appropriate members of management of the firm (including those charged with responsibility for quality management), possibly to the network or to external parties (subject to legal or regulatory prohibitions).
Independence			
11	The engagement partner shall form a conclusion on compliance with independence requirements that apply to the audit engagement. In doing so, the engagement partner shall: (Ref: Para. A5) (a) Obtain relevant information from the firm and, where applicable, network firms, to identify and evaluate circumstances and	Discussions and proposed changes still under consideration by the Task Force	*Further changes to be considered as necessary arising from revisions to ISQC 1.*

ISA 220 Para ref.	ISA 220 Current Requirements	Proposed Enhancements to Requirements	Matters for Further Consideration / Reference to Relevant Paragraph in the Issues Paper (Agenda Item 5-A)
	relationships that create threats to independence; (b) Evaluate information on identified breaches, if any, of the firm's independence policies and procedures to determine whether they create a threat to independence for the audit engagement; and (c) Take appropriate action to eliminate such threats or reduce them to an acceptable level by applying safeguards, or, if considered appropriate, to withdraw from the audit engagement, where withdrawal is possible under applicable law or regulation. The engagement partner shall promptly report to the firm any inability to resolve the matter for appropriate action. (Ref: Para. A6–A7)		
Acceptance and Continuance of Client Relationships and Audit Engagements			
12	The engagement partner shall be satisfied that appropriate procedures regarding the acceptance and continuance of client relationships and audit engagements have been followed, and shall determine that conclusions reached in this regard are appropriate. (Ref: Para. A8–A9)	The engagement partner shall be satisfied that appropriate procedures regarding the acceptance and continuance of client relationships and audit engagements have been followed~~, and shall~~. In doing so and in order to determine that the conclusions reached in this regard are appropriate~~.~~ for the audit, the engagement partner shall:	*Refer to paragraphs 59–61 within Issues Paper* Application material to be revised or developed to: • Distinguish between the acceptance and continuation of an audit engagement (i.e., to acknowledge

ISA 220 Para ref.	ISA 220 Current Requirements	Proposed Enhancements to Requirements	Matters for Further Consideration / Reference to Relevant Paragraph in the Issues Paper (Agenda Item 5-A)
		(a) Understand the firm's policies and procedures related to the acceptance and continuance of engagements, and how they have been applied for the audit engagement for which the engagement partner is responsible (including understanding important considerations relevant to the final conclusions reached); (b) Determine whether the firm's policies and procedures have resulted in the appropriate conclusion being reached for the audit engagement, or a different conclusion regarding acceptance or continuance of the client relationship and audit engagement should have been reached (including whether the engagement should have been accepted on different terms) and therefore whether further action is necessary at either the engagement level or firm level; (c) Respond to the need for further action by taking appropriate action at the engagement level, or communicate as necessary with the firm to determine the appropriate action to take; and (d) Communicate any other matters of relevance related to the acceptance or continuance of the client and audit	that there might be more information available for a continuance decision, but regardless, the acceptance decision should be made on the most informed basis possible). • Include application guidance to reinforce that the acceptance/continuance decision should be made on the most informed basis possible, including consideration of the nature of the entity, the industry within which it operates, likely complexities arising from the application of the requirements of the applicable financial reporting framework. Highlight the importance of consideration of any other issues that will be relevant to how the other elements of this ISA will need to be addressed – including for example issues regarding access to management information, members of the engagement team or others involved in the audit. An understanding of all of these matters forms the foundation for applying quality management principles when

ISA 220 Para ref.	ISA 220 Current Requirements	Proposed Enhancements to Requirements	Matters for Further Consideration / Reference to Relevant Paragraph in the Issues Paper (Agenda Item 5-A)
		engagement to the firm and engagement team as appropriate.	addressing the other requirements of ISA 220. • Cross reference to ISA 315 (Revised), paragraph 7 to reinforce that matters relevant to the acceptance/continuance decision will also likely be relevant to identifying and assessing risks of material misstatement, including information considered by the firm in making the conclusions and communicated the to the engagement partner. • Illustrate the application of the requirements to specific situations, potentially including examples of a situation where subsequent information indicates that the engagement should not have been accepted. This application guidance would also include highlighting the requirements of other ISAs as applicable.
13	If the engagement partner obtains information that would have caused the firm to decline the audit engagement had that information been available earlier, the engagement partner shall communicate that information promptly to the	If the engagement partner obtains information that would have caused the firm to decline, or not to continue, the audit engagement had that information been available earlier, the engagement partner shall, in a timely manner,	*Refer to paragraphs 59–61 within Issues Paper* Application guidance to highlight how additional information may come to the

ISA 220 Para ref.	ISA 220 Current Requirements	Proposed Enhancements to Requirements	Matters for Further Consideration / Reference to Relevant Paragraph in the Issues Paper (Agenda Item 5-A)
	firm, so that the firm and the engagement partner can take the necessary action. (Ref: Para. A9)	communicate that information ~~promptly~~ to the firm, so that the firm and the engagement partner can take the necessary action. (Ref: Para. A9)	auditor's attention throughout the course of the engagement.
Determination of Necessary Engagement Resources, Including Assignment Engagement Teams			
14	The engagement partner shall be satisfied that the engagement team, and any auditor's experts who are not part of the engagement team, collectively have the appropriate competence and capabilities to: (a) Perform the audit engagement in accordance with professional standards and applicable legal and regulatory requirements; and (b) Enable an auditor's report that is appropriate in the circumstances to be issued. (Ref: Para. A10–A12)	14. The engagement partner shall be satisfied that the audit engagement has adequate and appropriate resources necessary to perform the audit. In doing so, and in order to determine that the conclusions reached in this regard are appropriate for the audit, the engagement partner shall: (a) Understand the firm's policies and procedures related to establishing, obtaining or maintaining sufficient and appropriate resources in order for the engagement team to effectively undertake the engagement, including any specific requirements related to the assignment of the engagement team and particular resources that are to be used or involved in performing the audit. (b) Determine whether the firm's resources are sufficient and effective for the particular audit, or whether further risks to quality exist such that additional resources are required;	*Refer to paragraphs 62–64 within Issues Paper* • Application guidance to explain that resources is broader than just the personnel that will be involved, i.e., also include things like the audit methodologies, tools, templates and software. • Consider application material to explain further that the engagement partner needs to satisfied that the resources are available from the firm, understand the expectation of the firm relative to the use of the resources (including what might need to be done at the engagement level), and confirm the suitability of the resources for the engagement. • Consider application guidance to specifically address ADMs and use of data analytics.

ISA 220 Para ref.	ISA 220 Current Requirements	Proposed Enhancements to Requirements	Matters for Further Consideration / Reference to Relevant Paragraph in the Issues Paper (Agenda Item 5-A)
		(c) Respond to any further risks to quality by undertaking further actions as appropriate to obtain the necessary resources; and (d) Communicate matters of relevance related to the resources for the engagement to the firm and engagement team as appropriate.	
		14A. In applying the requirement in paragraph 14, the engagement partner shall be satisfied that: (a) The engagement team, and any auditor's experts who are not part of the engagement team, collectively have the appropriate competence and capabilities to: (i) Perform the audit engagement in accordance with professional standards and applicable legal and regulatory requirements; and (ii) Enable an auditor's report that is appropriate in the circumstances to be issued. (Ref: Para. A10–A12) (b) Any relevant or required firm methodologies, or technologies, are available and appropriate for the engagement, and that the engagement team members have the appropriate	*Refer to paragraphs 64 within Issues Paper* Application material to be developed to provide examples of different engagement team structures, such as when members of the engagement team are situated at ADMs, and how relevant individuals will need to collectively have the appropriate competence and capabilities. In addition, examples of relevant methodologies or technologies could include situations where data analytics are used to perform audit procedures. The Task Force also continues to consider issues around experts or individuals with specialized skills who are considered part of the engagement team, and whether external experts engaged by the auditor should be part of

ISA 220 Para ref.	ISA 220 Current Requirements	Proposed Enhancements to Requirements	Matters for Further Consideration / Reference to Relevant Paragraph in the Issues Paper (Agenda Item 5-A)
		skills and experience to use them as intended	the engagement team (see paragraph 96 of the Issues Paper)
Engagement Performance			
Direction, Supervision, ~~and~~ Performance and Reviews			
15	The engagement partner shall take responsibility for: (a) The direction, supervision and performance of the audit engagement in compliance with professional standards and applicable legal and regulatory requirements; and (Ref: Para. A13–A15, A20) (b) The auditor's report being appropriate in the circumstances.	15. In managing and achieving quality for the engagement, ~~T~~the engagement partner ~~shall take responsibility is responsible~~ for the performance of the engagement in compliance with professional standards and applicable legal and regulatory requirements, and the auditor's report being appropriate in the circumstances. In order to have an appropriate basis for demonstrating how the requirements of this ISA have been met, the engagement partner shall be sufficiently involved in the audit engagement, through appropriate: (a) ~~The d~~Direction~~,~~ and supervision of the engagement team and others involved in the audit ~~and performance of the audit engagement in compliance with professional standards and applicable legal and regulatory requirements~~; and (Ref: Para. A13–A15, A20) (b) ~~The auditor's report being appropriate in the circumstances.~~ Reviews of the audit	*Refer to paragraphs 65–74 within Issues Paper* Application guidance to be considered as discussed in **Agenda Item 5-A,** including factors that influence the nature, timing and extent of the EP's involvement and illustrative examples about how to apply them as described in paragraph 68.

ISA 220 Para ref.	ISA 220 Current Requirements	Proposed Enhancements to Requirements	Matters for Further Consideration / Reference to Relevant Paragraph in the Issues Paper (Agenda Item 5-A)
		documentation. (Ref: Para. A16–A17, A20) 15A [NEW]. In determining the nature, timing and extent of appropriate direction, supervision and review by the engagement partner, other members of the engagement team and others involved in the audit, the engagement partner shall : (a) Understand the firm's policies or procedures related to the direction, supervision and review of an audit engagement, including any policies and procedures applicable to the engagement; (b) Determine whether the firm's policies and procedures are sufficient and effective for the audit engagement, or whether further risks to quality exist; (c) Respond to the risks to quality by planning further direction, supervision and review for the engagement, including implementing the firm's policies and procedures relating to direction, supervision and review; and (d) Communicate matters of relevance related to the direction, supervision or review of the engagement to the firm and engagement team and others involved in the audit as appropriate.	

ISA 220 Para ref.	ISA 220 Current Requirements	Proposed Enhancements to Requirements	Matters for Further Consideration / Reference to Relevant Paragraph in the Issues Paper (Agenda Item 5-A)
~~*Reviews*~~			
16	The engagement partner shall take responsibility for reviews being performed in accordance with the firm's review policies and procedures. (Ref: Para. A16–A17, A20)	~~The engagement partner shall take responsibility for reviews being performed in accordance with the firm's review policies and procedures. (Ref: Para. A16–A17, A20)~~	*Refer to paragraphs 65–74 within Issues Paper* Note: See above, paragraph 16 has been combined with paragraph 15.
17	On or before the date of the auditor's report, the engagement partner shall, 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. (Ref: Para. A18–A20).	In applying the requirement in paragraph [15], the engagement partner shall, o~~O~~n or before the date of the auditor's report, ~~the engagement partner shall~~, and 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. (Ref: Para. A18–A20) To allow significant matters to be resolved on a timely basis to the engagement partner's satisfaction, the engagement partner shall review audit documentation that includes: (a) Critical areas of judgment, especially those relating to difficult or contentious matters identified during the course of the engagement; (b) Significant risks; and (c) Other areas the engagement partner considers important.	*Refer to paragraphs 65–74 within Issues Paper* Application guidance to be considered as discussed in paragraph 70 of **Agenda Item 5-A**.

ISA 220 Para ref.	ISA 220 Current Requirements	Proposed Enhancements to Requirements	Matters for Further Consideration / Reference to Relevant Paragraph in the Issues Paper (Agenda Item 5-A)
Consultation			
18	The engagement partner shall: (a) Take responsibility for the engagement team undertaking appropriate consultation on difficult or contentious matters; (b) Be satisfied that members of the engagement team have undertaken appropriate consultation during the course of the engagement, both within the engagement team and between the engagement team and others at the appropriate level within or outside the firm; (c) Be satisfied that the nature and scope of, and conclusions resulting from, such consultations are agreed with the party consulted; and (d) Determine that conclusions resulting from such consultations have been implemented. (Ref: Para. A21–A22)	The engagement partner shall~~:~~ ~~(a) T~~take responsibility for the engagement team undertaking appropriate consultation on difficult or contentious matters~~;~~. In doing so, and in order to determine that the conclusions reached in this regard are appropriate, the engagement partner shall: (a) Understand the firm's policies and procedures related to consultation on difficult and contentious matters; (b) Determine whether the firm's policies and procedures result in appropriate consultation being undertaken for the audit engagement, or whether further risks to quality exist such that additional consultation is necessary; (c) Respond to any further risks to quality by undertaking further consultations as appropriate; and (d) Communicate matters of relevance related to consultation on difficult or contentious matters to the firm and engagement team as appropriate, in particular, where relevant that: • ~~Be satisfied that m~~Members of the engagement team have undertaken	*Refer to paragraphs 75–76 within Issues Paper* *Further changes to be considered as necessary arising from revisions to ISQC 1.*

ISA 220 Para ref.	ISA 220 Current Requirements	Proposed Enhancements to Requirements	Matters for Further Consideration / Reference to Relevant Paragraph in the Issues Paper (Agenda Item 5-A)
		appropriate consultation during the course of the engagement, both within the engagement team and between the engagement team and others at the appropriate level within or outside the firm; • ~~Be satisfied that~~ tThe nature and scope of, and conclusions resulting from, such consultations are agreed with the party consulted; and • ~~Determine that the c~~Conclusions resulting from such consultations have been implemented. (Ref: Para. A21–A22)	
Engagement Quality Control Reviews			
19	For audits of financial statements of listed entities, and those other audit engagements, if any, for which the firm has determined that an engagement quality control review is required, the engagement partner shall: (a) Determine that an engagement quality control reviewer has been appointed; (b) Discuss significant matters arising during the audit engagement, including those identified during the engagement quality control review, with the engagement quality control reviewer; and	Discussions and proposed changes still under consideration by the Task Force	*Refer to paragraph 77 within Issues Paper* Further discussion on engagement quality control reviews to be progressed before changes to ISA 220 are considered in this regard. The Task Force is, however, of the view that regardless of whether the requirements relating to the selection of the EQCR and the performance of the review are set forth in a separate standard, the responsibilities of the engagement

ISA 220 Para ref.	ISA 220 Current Requirements	Proposed Enhancements to Requirements	Matters for Further Consideration / Reference to Relevant Paragraph in the Issues Paper (Agenda Item 5-A)
	(c) Not date the auditor's report until the completion of the engagement quality control review. (Ref: Para. A23–A25)		partner (as set forth in extant ISA 220, paragraph 19 and amended as necessary) should remain in ISA 220.
20	The engagement quality control reviewer shall perform an objective evaluation of the significant judgments made by the engagement team, and the conclusions reached in formulating the auditor's report. This evaluation shall involve: (a) Discussion of significant matters with the engagement partner; (b) Review of the financial statements and the proposed auditor's report; (c) Review of selected audit documentation relating to the significant judgments the engagement team made and the conclusions it reached; and (d) Evaluation of the conclusions reached in formulating the auditor's report and consideration of whether the proposed auditor's report is appropriate. (Ref: Para. A26–A27, A29–A31)	Discussions and proposed changes still under consideration by the Task Force	See comment above. Further discussion on engagement quality control reviews to be progressed before changes to ISA 220 are considered in this regard.
21	For audits of financial statements of listed entities, the engagement quality control reviewer, on performing an engagement quality control review, shall also consider the following:	Discussions and proposed changes still under consideration by the Task Force	See comment above. Further discussion on engagement quality control reviews to be progressed before changes to ISA 220 are considered in this regard.

ISA 220 Para ref.	ISA 220 Current Requirements	Proposed Enhancements to Requirements	Matters for Further Consideration / Reference to Relevant Paragraph in the Issues Paper (Agenda Item 5-A)
	(a) The engagement team's evaluation of the firm's independence in relation to the audit engagement; (b) Whether appropriate consultation has taken place on matters involving differences of opinion or other difficult or contentious matters, and the conclusions arising from those consultations; and (c) Whether audit documentation selected for review reflects the work performed in relation to the significant judgments and supports the conclusions reached. (Ref: Para. A28–A31)		
Differences of Opinion			
22	If differences of opinion arise within the engagement team, with those consulted or, where applicable, between the engagement partner and the engagement quality control reviewer, the engagement team shall follow the firm's policies and procedures for dealing with and resolving differences of opinion.	The engagement partner shall take responsibility for determining that ~~If differences of opinion arise within the engagement team, with those consulted or, where applicable, between the engagement partner and the engagement quality control reviewer, the engagement team shall follow~~ the firm's policies or procedures for dealing with and resolving differences of opinion ~~have~~ have been complied with. In doing so, and to determine that the conclusions reached in this regard are appropriate, the engagement partner shall:	*Refer to paragraphs 75–76 within Issues Paper* Consider the need for additional application guidance as changes to ISQC 1 are progressed.

ISA 220 Para ref.	ISA 220 Current Requirements	Proposed Enhancements to Requirements	Matters for Further Consideration / Reference to Relevant Paragraph in the Issues Paper (Agenda Item 5-A)
		(a) Understand the firm's policies and procedures related to dealing with and resolving differences of opinion; (b) Determine whether the firm's policies and procedures result in appropriate resolution of differences of opinion that have arisen during the audit engagement, or whether further risks to quality exist such that additional action is necessary; (c) Respond to any further risks to quality by undertaking further actions as appropriate; and; (d) Communicate matters of relevance related to dealing with and resolving differences of opinion to the firm and engagement team as appropriate.	
Monitoring			
23	An effective system of quality control includes a monitoring process designed to provide the firm with reasonable assurance that its policies and procedures relating to the system of quality control are relevant, adequate, and operating effectively. The engagement partner shall consider the results of the firm's monitoring process as evidenced in the latest information circulated by the firm and, if applicable, other network firms and whether	To be progressed as the revision to ISQC 1 is progressed.	*Refer to paragraphs 78–79 within Issues Paper* Consider the need for additional application guidance as changes to ISQC 1 are progressed.

ISA 220 Para ref.	ISA 220 Current Requirements	Proposed Enhancements to Requirements	Matters for Further Consideration / Reference to Relevant Paragraph in the Issues Paper (Agenda Item 5-A)
	deficiencies noted in that information may affect the audit engagement. (Ref: Para A32–A34)		
Overall Stand-back Before Concluding that Quality has been Effectively Managed at the Engagement Level [NEW]			
23A [NEW]	N/A	23A [NEW] Prior to forming an opinion on the financial statements, the engagement partner shall conclude that quality has been effectively managed for the engagement. In forming this conclusion, the engagement partner shall evaluate whether all risks to quality have been appropriately identified, and addressed including as they relate to the core elements of this ISA. Additionally, the EP shall evaluate whether there are any additional quality risks relevant to the audit engagement and if so, plan and perform additional responses to address such risks.	*Refer to paragraphs 80–83 within Issues Paper*
Documentation			
24	The auditor shall include in the audit documentation: (a) Issues identified with respect to compliance with relevant ethical requirements and how they were resolved. (b) Conclusions on compliance with independence requirements that apply to the audit engagement, and any relevant	Discussions and proposed changes still under consideration by the Task Force	Documentation requirements to be discussed once other principles in the standard are agreed. Refer to paragraph 35 within the Issues Paper.

ISA 220 Para ref.	ISA 220 Current Requirements	Proposed Enhancements to Requirements	Matters for Further Consideration / Reference to Relevant Paragraph in the Issues Paper (Agenda Item 5-A)
	discussions with the firm that support these conclusions. (c) Conclusions reached regarding the acceptance and continuance of client relationships and audit engagements. (d) The nature and scope of, and conclusions resulting from, consultations undertaken during the course of the audit engagement. (Ref: Para. A35)		
25	The engagement quality control reviewer shall document, for the audit engagement reviewed, 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 on or before the date of the auditor's report; and (c) The reviewer is not aware of any unresolved matters that would cause the reviewer to believe that the significant judgments the engagement team made and the conclusions it reached were not appropriate.	Discussions and proposed changes still under consideration by the Task Force	Further discussion on engagement quality control reviews to be progressed before changes to ISA 220 are considered in this regard.

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Meeting: IAASB

Meeting Location: New York, USA

Meeting Date: June 19–22, 2017

Agenda Item 7

Group Audits

Objectives of Agenda Item

1. The objectives of this Agenda item are:

   - To inform the IAASB about the issues that have been discussed by the Group Audits Task Force (GATF) relating to International Standard on Auditing (ISA) 600,[1] including the relationships among and between the Group Audits project and other IAASB projects; and
   - To obtain the IAASB's views on the way forward with respect to the Group Audits project.

GATF

2. The GATF comprises the following members:

   - Megan Zietsman, IAASB Deputy Chair and Task Force Co-Chair;
   - Bob Dohrer, IAASB Member and Task Force Co-Chair;
   - Len Jui, IAASB Member;
   - Wolf Böhm, IAASB Technical Advisor; and
   - Josephine Jackson, IAASB Technical Advisor.

Background

3. At the September 2016 IAASB and the IAASB Consultative Advisory Group (CAG) meetings, the Group Audits Working Group provided proposals for potential revisions to ISA 600 to enhance the application of a risk-based approach to the scoping of a group audit.

4. In December 2016, the IAASB approved a project proposal[2] for the revision of ISA 600 to strengthen the auditor's approach to planning and performing a group audit and to clarify the interaction of ISA 600 with the other ISAs.

Activities of the GATF

5. The GATF has had two physical meetings since the December 2016 IAASB meeting to progress the project, including a discussion of the following issues:

   - Scoping of a group audit engagement, including:

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1 ISA 600, *Special Consideration—Audits of Group Financial Statements (Including the Work of Component Auditors)*

2 *Enhancing Audit Quality: Project Proposal for the Revision of the IAASB's International Standards Relating to Quality Control and Group Audits*

- Obtaining an understanding of the group and its components (including the structure of the group and use of shared service centers);
- Obtaining an understanding of the component auditor and determining the extent of involvement by the group engagement team in the work of the component auditor;
- Identifying and assessing the risks of material misstatement; and
- Responding to identified risks of material misstatement.

The GATF discussed how alternative approaches to scoping an audit engagement would work with different group structures, including consideration of how to apply a more top-down approach.

- Acceptance and continuance, including:
  - Placing particular focus on identifying prior to acceptance and to the extent possible, situations where there may be difficulty in obtaining sufficient appropriate audit evidence, including where access to audit evidence or component auditors may be restricted; and
  - Considerations regarding the terms of engagement.
- Communications between the group engagement team and the component auditors, including the communication of non-compliance with laws and regulation in light of recent revisions to the Code of Ethics for Professional Accountants of the International Ethics Standards Board for Accountants in this regard.
- The necessary work effort of the group engagement team in relation to the consolidation process, particularly regarding sub-consolidations.
- Group audits involving component auditors when the component auditor is from within the group engagement team`s network versus when the component auditor is from outside the network.

Interaction with Other Projects

6. In the project proposal the IAASB recognized that there is a strong linkage between ISA 600 and other International Standards, in particular ISQC 1[3], ISA 220,[4] and ISA 315 (Revised).[5]

7. In the course of the GATF's discussions, it became clear that some of the key issues being addressed by the GATF are incremental to issues being considered in connection with other IAASB projects. That is, a basic issue may be addressed in one standard but the unique application of that standard in a group audit scenario needs to be addressed in ISA 600. The GATF is of the view that in some cases, the more detailed requirements will be included in other ISAs (for example, in ISA 220 or ISA 315 (Revised)), and the content in ISA 600 would be focused more on guidance on how to apply the requirements to group audits. Following are examples of the overlap between other International Standards and ISA 600:

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[3] International Standard on Quality Control (ISQC) 1, *Quality Control for Firms that Perform Audits and Reviews of Financial Statements, and Other Assurance and Related Service Engagements*

[4] ISA 220, *Quality Control for an Audit of Financial Statements*

[5] ISA 315 (Revised), *Identifying and Assessing the Risks of Material Misstatement through Understanding the Entity and Its Environment*

- Issues related to the acceptance and continuance of an engagement, communications, direction, supervision and review (ISQC 1 and ISA 220);
- Issues related to identification and assessment of risks of material misstatement (including significant risks), consideration of internal control (including identifying and understanding controls relevant to the audit), and consideration of information technology and related risks (ISA 315 (Revised)).

8. Also, as described in **Agenda Item 4-A**, the overarching requirements regarding consideration and use of network level functions by firms in relation to firm's systems of quality management would be established in ISQC 1, with further consideration at the engagement level being addressed in ISA 220. ISA 600 would then 'build' on those standards for the aspects that would be particular to group audit situations, potentially mainly through application material that would provide further guidance for those specific aspects (e.g., assessing the competence of component auditors).[6]

Way Forward

9. Although the GATF has discussed many ISA 600–specific issues since the last IAASB discussion, the GATF has noted that the nature of the public interest issues at hand has given rise to a need for the GATF to engage more directly with the Quality Control Task Force (QCTF), ISA 220 Task Force (ISA 220 TF) and ISA 315 (Revised) Task Force (ISA 315 (Revised) TF) to help formulate the overarching requirements in those standards. These requirements, in turn, will become the building blocks to dealing with group audit specific matters within ISA 600.

10. While the GATF has made progress on some issues that are specific to ISA 600 (such as possible enhancements to the approach to the scoping of the group audit, a possible way forward for the approach to equity method investments, and sub-consolidations), the GATF proposes that it continue to prioritize engaging directly with the QCTF, ISA 220 TF and ISA 315 (Revised) TF to provide appropriate input regarding the connection points between those projects and ISA 600.

11. A presentation will be given to the IAASB on the GATF discussions to date on these matters and the way forward for the GATF, which will take into account any feedback received from the Steering Committee meeting on June 19th, 2017.

Matter for IAASB Consideration

1. The IAASB is asked for its views on the interrelationships and dependencies between ISA 600 and the projects to revise ISQC 1, ISA 220, and ISA 315 (Revised) as discussed above, and how the GATF should proceed.

Material Presented

A presentation will be provided during the Board week.

[6] The issues related to networks have been dealt with in a separate paper—see Agenda Item 4-A. Group audit issues include concerns about a group engagement team placing reliance on the firm or network quality control policies and procedures without due consideration of an appropriate basis for doing so.

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Meeting: IAASB

Meeting Location: New York, USA

Meeting Date: June 19–22, 2017

Agenda Item 4

Consideration of Networks—Issues and Discussion

Objective of Agenda Item

1. The objective of this Agenda Item is to obtain the IAASB's feedback on the matters set out by the Quality Control Task Force (QCTF), the ISA 220[1] Task Force (TF) and the Group Audits Task Force (GATF) (hereinafter: the Task Forces) on 'network'[2] related matters relevant to the projects addressing proposed revisions to:

   - International Standard on Quality Control (ISQC) 1, *Quality Control for Firms that Perform Audits and Reviews of Financial Statements, and Other Assurance Engagements and Related Services Engagements;*
   - ISA 220; and
   - ISA 600, *Special Considerations—Audits of Group Financial Statements (Including the Work of Component Auditors).*

2. The Task Forces comprise the following members:

QCTF	ISA 220 TF	GATF
• Karin French, IAASB Member and Chair of the QCTF • Bob Dohrer, IAASB Member • Brendan Murtagh, IAASB Member • Imran Vanker, IAASB Member • Josephine Jackson, IAASB Technical Advisor • Denise Weber, IAASB Technical Advisor • Keith Wilson, US Public Company Accounting Oversight Board (Official Observer)	• Megan Zietsman, IAASB Member and Chair of the ISA 220 TF • Karin French, IAASB Member • Rich Sharko, IAASB Member • Imran Vanker, IAASB Member • Brendan Murtagh, IAASB Member • Josephine Jackson, IAASB Technical Advisor • Annette Köhler, IAASB Member (correspondent member)	• Megan Zietsman, IAASB Member and Co-Chair of the GATF • Bob Dohrer, IAASB Member and Co-Chair of the GATF • Len Jui, IAASB Member • Wolf Böhm, IAASB Technical Advisor • Josephine Jackson, IAASB Technical Advisor

[1] International Standards on Auditing (ISA) 220, *Quality Control for an Audit of Financial Statements*

[2] Firms may operate through arrangements that share common quality control policies and procedures and common methodologies, but the extent of sharing can vary significantly. For the purposes of this Agenda Item "network" is used to describe those arrangements where firms share common quality control policies and procedures, including monitoring and inspection procedures, and common methodologies.

QCTF	ISA 220 TF	GATF
• Dawn McGeachy, IFAC Small and Medium Practices Committee Representative (correspondent member)		

Activities of the Task Forces

3. With the exception of providing high-level feedback from the responses to the Invitation to Comment (ITC), *Enhancing Audit Quality: A Focus on Professional Skepticism, Quality Control and Group Audits* to the IAASB at the September 2016 meeting, the Board has not discussed matters related to networks specifically. The IAASB's Consultative Advisory Group last discussed this topic in the development of the ITC.

4. There have been no specific meetings or call of the Task Forces related to this topic, rather it has been discussed as part of the meetings and teleconferences held by the various Task Forces—details of those meetings and calls can be found in Agenda Items 2, 5 and 7 respectively. The QCTF and ISA 220 TF had a joint discussion on the matters set out in **Agenda Item 4–A** in April 2017.

5. Representatives of the IAASB discussed network-related matters, including a broad overview of the proposed approach described in **Agenda Item 4–A**, with members of the Forum of Firms at their May 2017 meeting.

Matters for IAASB Consideration

6. **Agenda Item 4–A** presents the discussions and views of the Task Forces, setting out matters for IAASB consideration. The IAASB is asked to consider the matters as set out in the agenda item and provide input to assist the Task Forces in progressing the changes in the relevant standards.

7. The **Supplement to Agenda Item 2** includes a summary of the responses to the ITC, as well as the names of the respondents to the ITC.

Material Presented

Agenda Item 4-A	*Further Consideration of Networks–Issues and Discussion*
Supplement to Agenda Item 2	*Summary of Responses to the ITC*

Consideration of Networks[1]—Issues and Discussion

Objective of the IAASB Discussion

The objective of this Agenda Item is to obtain the IAASB's feedback on the matters set out below from the Quality Control Task Force (QCTF), the ISA 220[2] Task Force and the Group Audits Task Force (GATF) (hereafter the 'Task Forces')[3] on 'network' related matters.

A. Introduction

1. Paragraph 54 of ISQC 1 refers to the fact that some firms operate as part of a 'network of firms.' Firms are organized under many different arrangements that may or may not meet the current definition of a network in the International Ethics Standards Board for Accountants' (IESBA) *Code of Ethics for Professional Accountants* (the IESBA Code)[4] and the IAASB's International Standards (i.e., ISQC 1 and the ISAs). Currently, the IAASB's International Standards do not establish requirements for firms at the network level nor do they address in any significant detail a firm's ability to place reliance on network policies or procedures to address firm-level or engagement-level responsibilities for quality management.

2. Regulators and audit oversight bodies have expressed concerns related to networks, with issues being highlighted in their inspection findings. In particular, regulators and audit oversight bodies have noted that:

   - Firms, in some circumstances, may seek to rely on a network's system of quality control to address some of the firm's responsibilities established by ISQC 1, without sufficient basis for doing so.
   - ISQC 1 only makes brief reference to monitoring procedures that may, or may not be, performed at the network level.[5]

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1 For the purposes of this Agenda Item, the term 'network' is used to describe larger structures that meet the network definition in ISQC 1, and the term 'network activities' is used in the context of policies, procedures and other activities in place or performed at the network-level that may be relevant to the firm`s quality management (see paragraph 12).

2 International Standards on Auditing (ISA) 220, *Quality Control for an Audit of Financial Statements*

3 The issues and possible actions relating to networks set out in this Agenda Item have been discussed by the Task Forces, including a joint discussion by the QCTF and ISA 220 Task Force in April 2017. The Task Forces continue to work together on these matters as they relate to possible actions that are interrelated between the projects to revise International Standard on Quality Control (ISQC) 1, *Quality Control for Firms that Perform Audits and Reviews of Financial Statements, and Other Assurance Engagements and Related Services Engagements*, ISA 220 and ISA 600, *Special Considerations—Audits of Group Financial Statements (Including the Work of Component Auditors)*.

4 For the purpose of this Agenda Item, references are made to the provisions in the extant IESBA Code. As part of the Structure of the Code Project, restructuring revisions have been made to those extant provisions, including to those that are relevant to "networks" or "network firms." The restructuring revisions are not however intended to change the meaning of the provisions in the extant Code.

5 See paragraph 54 of ISQC 1

- Networks that carry out inspections of individual firms, as part of their monitoring procedures, do not always adequately consider the implications of those findings, including the impact of those findings on other firms within the network.
- Their ability to access audit documentation of other firms in the network, including the ability of the firms within the network to share information with regulators and audit oversight bodies, is limited or difficult in some cases.[6]

3. In addition, questions have arisen about whether, how, under what circumstances, and to what extent engagement teams can rely on common systems of quality control when using work performed by other auditors from the same firm or a network firm (e.g., in group audit situations).

4. For example, the group engagement team's involvement in the work performed by the component auditor that is not part of the network may need to be different, and the nature and timing of such involvement may also need to be different, when they are not subject to, for example, the same quality control policies and procedures or methodologies. For example, depending on the circumstances, more detailed instructions, and more frequent and more in-person communications between the group engagement team and component auditors may be necessary as the audit progresses.

5. As noted above, issues related to networks could affect management of quality by the firm (i.e., ISQC 1) and at the engagement level (i.e., ISA 220 and ISA 600). The IAASB therefore included the issues relating to networks in the ITC, setting out the identified issues at both the firm and engagement level. In presenting these issues, the IAASB recognized that networks have significantly different structures and it would therefore likely be challenging to develop standards that would be effective in addressing this broad range of arrangements. Further, it was acknowledged that networks' structures, and the way that firms within the networks interact, continue to evolve and any standard-setting actions to address issues related to networks needed to remain principle-based and able to be applied to evolving circumstances. The ITC sections addressing networks, including the possible actions to address the identified issues relating to networks are set out in Appendix A.

6. The responses to the ITC confirmed the issues and concerns, and encouraged the IAASB to further explore these matters by considering changes to the IAASB's International Standards as appropriate. Respondents highlighted the importance of the relationship between networks and their member firms, and the potential implications of such relationships on audit quality. Respondents also emphasized the need for, and the importance of, actions for ISQC 1 to be strengthened in relation to consideration of inspections that have taken place across networks, and related communications. A summary of the responses to the ITC can be found in the Supplement to Agenda Item 2.

7. The IAASB approved a project proposal to commence projects to revise ISQC 1, ISA 220 and ISA 600 at its December 2016 meeting.

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[6] This issue was included in the Invitation to Comment (ITC), *Enhancing Audit Quality in the Public Interest: A Focus on Professional Skepticism, Quality Control and Group Audits* as feedback from regulators and audit oversight bodies, however standard-setting will not be able to address this matter as it relates to restrictions imposed by jurisdictional laws and regulations. Therefore, it will not be explicitly addressed as part of the projects to revise ISQC1, ISA 220 and ISA 600. However, when dealing with risks relating to a firm's compliance with relevant laws and regulations in ISQC 1, it may be appropriate to include as an example, law or regulation within a jurisdiction that requires firms affirm that regulators will be able to gain access to working papers and personnel as a condition of licensing or registration.

8. With the exception of providing high-level feedback from the ITC responses at the September 2016 IAASB meeting, the IAASB has not had further discussions about the topic of networks since the ITC was issued. The last discussion by the IAASB's Consultative Advisory Group (CAG) on this topic was during the development of the ITC (see relevant minutes in Appendix B). Representatives of the IAASB discussed network related matters, including the broad approach described in this Agenda Item, with members of the Forum of Firms (FoF) at their May 2017 meeting. The FoF's members were broadly supportive of the direction, and encouraged the IAASB to continue to consider how networks are structured when making changes (i.e., to not develop requirements which would be difficult to implement because of the different structures of networks). They also further iterated the need for clarification on what the 'basis of reliance' should be when 'relying on' common policies and procedures.

What Is a Network?

9. The IAASB and the IESBA have a common definition of a network in their standards. The definition can be found in Appendix C, which also includes a summary of how networks are described or defined in certain other standards, laws or regulations.

10. The definition of a network in the IAASB's International Standards and the IESBA Code is very broad, and contemplates the wide variety of networks that may exist, comprising of larger structures that may share some, or all of, the following elements among the entities within the structure (see Appendix D for the discussion of Networks and Network Firms in the IESBA Code):

    - Use of a common brand name;
    - Common quality control policies and procedures;
    - Aimed at profit or cost sharing among the entities within the structure;
    - Common ownership, control or management;
    - Common business strategy; or
    - A significant part of professional resources (see below).

11. The IAASB's International Standards do not elaborate on 'professional resources' but the IESBA Code sets out the examples in paragraph 290.23 of the IESBA Code, including:

    - Common systems that enable firms to exchange information such as client data, billing and time records;
    - Partners and staff;
    - Technical departments that consult on technical or industry specific issues, transactions or events for assurance engagements;
    - Audit methodology or audit manuals; and
    - Training courses and facilities.

12. The definition of a network is well-established and accepted in both the IAASB's and IESBA's standards. It is the Task Forces' view that the approach described as follows for addressing the issues relating to networks can be applied in the context of the extant definition. The approach described is based on circumstances when the network has common policies and procedures, and not simply on whether or not there is a larger structure to which the firm belongs that meets the

current definition of network. The Task Forces also note that making any changes to the definition of a network would need to be coordinated with IESBA, i.e., in order to maintain consistency with how networks are defined in both the IAASB's International Standards and the IESBA Code. In the view of the Task Forces the issues around networks do not arise because of the definition of a network, and therefore the Task Forces are of the view that the definition does not need to be amended.

B. Activities Performed at the Network Level: Firm Responsibilities

13. Certain activities within a firm's system of quality management could be performed wholly or in part at a network level. Additionally, there may be common policies and procedures that are expected or required to be used by all firms within the network (network firms). For example:

- The network may develop the audit methodology and related audit software and require that they be used by all network firms.
- The network may establish policies and procedures related to independence that are expected to be implemented by each network firm. In addition, the network may implement systems at a network level to facilitate or contribute to the effective functioning of such policies and procedures at the firm level.
- The network may perform the monitoring of network firms' systems of quality management, including through the performance of periodic practice reviews and monitoring the results of external inspections of network firms.
- The network may establish technical resources to support the consultation process and to addressing differences of opinion that may arise between network firms.

In the rest of this paper, such matters as noted above are referred to collectively as "activities performed by the network."

Developing Network-Level Requirements

14. As previously noted, network arrangements and the activities performed by a network may vary significantly. Firms within a network are generally not owned or directly controlled by the network. The extent of operational and decision-making power at the network level can also vary among networks and enforcement powers in relation to individual network firms may be limited. Compliance at the network firm level with common quality control policies and procedures, and common methodologies, can be influenced through economic and other measures, but often cannot be centrally controlled at the network level.

15. The ITC acknowledged the challenges of trying to establish requirements in ISQC 1 at the network level, including that:

- Networks may be structured differently.
- The nature and extent of the common policies and procedures in networks will vary, likely significantly.
- Structures may be highly influenced by applicable law or regulation in the various jurisdictions in which networks and individual firms are established.

Nevertheless, the ITC asked for stakeholder views about whether requirements at the network level should be further considered by the IAASB.

16. Respondents to the ITC recognized the challenges associated with developing requirements at the network level in the IAASB's International Standards, and were generally therefore supportive of the IAASB taking action to address the issues at the firm level or engagement level (although a few were supportive of the establishment of requirements at the network level).[7] Those respondents who recognized the challenges of establishing requirements at the network level highlighted the varying network structures that exist and the inability of the IAASB to develop requirements that would be adaptable to the wide variety of circumstances that can and do arise in practice. However, there was strong support, across all stakeholder groups, for the IAASB to give further consideration to enhancements to the standards to clarify what a network firm's "basis of reliance" should be when relying on common policies and procedures at a network level (i.e., what needs to be done by network firms to demonstrate that what they are relying on has an appropriate basis and is operating as expected).

17. The Task Forces further considered the merits and consequences of establishing requirements at the network level in the IAASB's International Standards, and agreed that this would be challenging for various reasons and therefore unlikely to result in effectively addressing the issues identified. In particular, the Task Forces considered:

    - The different structures of networks (for example, varying common elements across networks, variances in the activities performed by networks, structures that are called networks that may not have common quality control policies and procedures, or significant differences in the nature and extent of the common policies and procedures and how these are implemented).
    - The different degrees of centralized control that exist across networks (including potentially very little in a larger structure referring to itself as a network without having common policies and procedures).
    - Difficulties that would arise with monitoring compliance with network-level requirements (especially by external oversight bodies), because of the multi-jurisdictional nature of networks and the firms within those networks being subject to different laws and regulations, including oversight by audit regulators.

Activities Performed by the Network Being Used by a Network Firm as Part of Its System of Quality Management

18. The Task Forces agreed with the ITC respondents that further consideration should be given to what a network firm should do in relation to information coming from the operation of network activities.

19. As described in the ITC, regulators and audit oversight bodies have raised concerns that in certain cases firms rely on network-level activities to address firm-level requirements, but without sufficient information about how those activities operate at a network level and about how effective they are. Consequently, firms may not be able to demonstrate their basis for relying on those activities (i.e., have been able to demonstrate that those activities are sufficiently effective for the intended purpose).

20. Complying with the requirements of ISQC 1 is the firm's responsibility. In circumstances when network activities are used by a network firm as part of addressing its risks to quality within the firm's

[7] Basel Committee on Banking Supervision, CFA Institute, The Investment Association, International Corporate Governance Network, Crowe Horwath International.

system of quality management, the Task Forces are of the view that the firm has a responsibility to proactively:

- Understand the network activities;
- Make a determination as to whether the network activities are relevant to, and support, the firm's system of quality management (i.e., whether they are relevant and effectively designed to address firm-level quality risks); and
- Consider information about the effectiveness of those activities (i.e., to support a conclusion that they are appropriate and effective in addressing firm-level quality risks).

21. Accordingly, the Task Forces recommend that ISQC 1 should be strengthened to address the responsibilities referred to in paragraph 20. These revisions to ISQC 1 would support a more proactive approach to considering and using information from network activities at the firm-level, and is consistent with the principles proposed by the QCTF in relation to the incorporation of a quality management approach in ISQC 1. The Task Forces are also of the view that this approach would:

    - Be adaptable to the different components of a firm's system of quality management (see paragraph 21 of **Agenda Item 2-B**).
    - Encourage more robust two-way communication between the firm and the network, which aligns to the proposals in the component "information, communication and documentation" in **Agenda Item 2-B**.
    - Be adaptable to the various types of networks as it would be up to a firm to determine whether and how the activities performed by the network would support the firm's system of quality management and address risks to quality at the firm level, i.e., the approach could be applied regardless of how a network is structured, or the extent to which the network adopts common policies and procedures.

22. In understanding the activities performed (as set out in paragraph 20 above) at a network level and in considering related information provided by the network, it would be the network firm's responsibility to evaluate whether those activities are appropriate and effective, and whether the network firm has sufficient information from the network to form the basis for the firm's conclusion. For example, in determining whether the audit methodology established by the network is appropriate and effective, the network firm will consider information provided by the network about matters such as:

    - The process of developing the audit methodology such that it complies with the ISAs and any network-level requirements, as well as details about the quality review processes that are undertaken in their development.
    - How the audit methodology is updated for changes in standards or network-level expectations, and how it is determined that any changes to the methodology are timely, complete and appropriate, including details about the quality review processes that are undertaken.

      The network firm may seek additional information from the network to assist in making a determination about the appropriateness and effectiveness of the audit methodology. Accordingly, the responsibility would be on the network firm for seeking additional information from the network as necessary. If the network is unable to provide the requested information about network activities, the network firm would then need to implement other actions to satisfy

itself about the appropriateness and effectiveness of the audit methodology. In this example, if the network could not provide the necessary information about how the audit methodology is developed and maintained, the firm would need to perform additional procedures at the firm level.

23. In designing its system of quality management, the network firm would consider the information about the network activities obtained from the network, including performing an evaluation of the appropriateness and effectiveness of these activities in addressing quality risks at the firm level. Accordingly, the necessary actions or responses at the firm level may differ depending on the network activities involved and the network firm's evaluation thereof. Furthermore, the firm would consider jurisdictional aspects (e.g., legal or regulatory requirements or local professional standards). For example, in relation to the audit methodology example above, the firm may determine that there is little, if any, further action required by the firm in order to use the network's methodology; however the firm may identify the need to perform additional firm-level activities to supplement the network methodology to appropriately address local jurisdictional requirements.

24. The firm may determine that a more detailed understanding is needed in relation to certain activities performed at a network level and therefore seek more information from the network in order to make appropriate conclusions at the firm level. For example:

- In the case of audit software, firms may seek an understanding of how the use of the tools has been vetted, including how the determination has been made that the tools are 'fit for purpose' and will function as intended. Network firm may also seek to understand what the expectations are about those processes and controls the firm needs to put in place around the deployment of such tools. Those expectations may include, for example, expectations relating to:
    - Proper deployment of, and controls over, the use of the software;
    - Having appropriate IT infrastructure in place to support the software;
    - Delivering the necessary training for engagement teams;
    - Communicating to engagement teams what they are expected to do in order to use the tools effectively; or
    - Providing technical support.
- In the case of network-level monitoring activities, network firms may seek to understand the nature, timing and extent of firm-level monitoring activities in relation to the various aspects of network firms' system of quality management, including how the results are communicated and whether they take account of all relevant information (including from external sources) on a timely basis. Firms might seek additional information about deficiencies identified, the causes of the deficiencies and what is being done to remediate them. These activities are likely particularly relevant to firms that make extensive use of other firms within the network when performing group audits.

25. In the view of the Task Forces, the inclusion of robust requirements directed at the firm to more proactively understand network-level activities and to consider or evaluate the information in the

context of information about such activities being used by the firm to comply with ISQC 1's firm-level requirements would:

(a) Strengthen what the network firm has to do in relation to network-level activities, including the related policies and procedures, and would cause the network firm to more actively consider and seek out relevant information from the network about such activities i.e., in order to provide the basis for how the firm's responses to quality risks are addressed by such activities and the related policies and procedures.

(b) Influence what the network does and what kind of information is provided to network firms within the network. For example, all the firms in the network would likely be requesting similar information from the network, which would in turn may drive the networks to more consistently provide the network firms with the necessary information on a transparent and timely basis. The Task Forces are therefore of the view that setting robust, clear requirements at the firm level for how the network-level activities and related policies and procedures should be considered by firms (i.e., as responses to quality risks within the overall system of firm-level quality management) will improve quality overall, which is clearly in the public interest.

C. Activities Performed at the Network Level: Engagement Team Responsibilities

26. At the engagement level, when managing quality, the engagement partner and the engagement team have the responsibility to understand the activities performed at the firm level that are relevant to managing quality at the engagement level. Extant ISA 220, paragraph 4 indicates that "Engagement teams are entitled to rely on the firm's system of quality control, unless information provided by the firm or other parties suggests otherwise." This paragraph is supported by application material (paragraph A2) that indicates that the engagement team may rely on the firm's system of quality control in relation to, for example:

- Competence of personnel through their recruitment and formal training.
- Independence though the accumulation and communication of relevant independence information.
- Maintenance of client relationships through acceptance and continuance systems.
- Adherence to applicable legal and regulatory requirements through the monitoring process.

As the Task Force continues to progress changes to ISA 220, and in light of the IAASB's views of the matters set out in this paper, the Task Force will make necessary revisions to these paragraphs in ISA 220.

27. Information from network firms is only addressed in extant ISA 220 in the context of:

- Complying with relevant independence requirements - paragraph 11 (a) of ISA 220 requires that the engagement partner obtain relevant information from the firm, and where applicable, the network firms, to identify and evaluate circumstances and relationships that create threats to independence.
- Considering the results of the firm's monitoring process – paragraph 23 of ISA 220 indicates that this would be as evidenced in the latest information circulated by the firm and, if applicable other network firms.

28. The proposed revisions to ISA 220 (see **Agenda Items 5-A** and **5-B**) involve more proactive consideration by engagement partners and engagement teams of the relevant firm-level activities, and information about their effectiveness relative to managing quality at the engagement-level – an approach that is very similar to that outlined in the section above as to how firms might consider network-level policies and procedures. The Task Forces also understand and agree that it would, for the most part, likely not be practical, nor efficient, for individual engagement partners and engagement teams to be required to seek information directly from the network about network activities and their effectiveness. The Task Forces therefore believe that, in general, consideration of network-level activities would likely be more relevant and appropriate to be conducted by the firm, with the firm then having the responsibility for distributing appropriate information to engagement partners and engagement teams. In the view of the Task Forces, the information distributed by the firm forms the basis for the engagement's partner's conclusions as to how quality is managed at the engagement level.

29. For example, networks may establish policies and procedures related to independence that are expected to be implemented by each network firm, and systems are implemented at a network level to facilitate or contribute towards the effective functioning of such policies and procedures. The network firm would likely implement the necessary firm-level policies and procedures and may have already obtained information about, and evaluated the effectiveness of, the operation of the information obtained from the network-level systems. In such cases it would likely be appropriate that this process is used as the basis for how risks related to compliance with relevant independence requirements are managed at the engagement level, and how this is monitored and remediated. However, in doing so, and consistent with other changes being considered in ISA 220, the engagement partner and engagement team would also consider whether there are other risks to quality relating to independence and whether any additional procedures are necessary at the engagement-level. For example, the engagement partner might determine that the network-level activity is not a sufficient response to the risk to quality at the engagement level, and might therefore decide to obtain positive confirmations from all team members directly (e.g., confirmations that they have read and understood the applicable independence requirements and that they are in compliance, or if not, that instances of possible or actual non-compliance have been brought to the attention of the engagement partner).

30. In some cases, it may be necessary for individual engagement partners or teams to base conclusions on how quality is managed at the engagement level that involve taking into account network-level activities that have not been otherwise evaluated or considered at the firm level, or where additional information is needed from the network about the effectiveness of the applicable network-level activities. In these cases, the engagement partner may ask the firm to request the necessary information from the network on behalf of the requesting partner or team. However, if the firm does not do so, then the engagement partner may find it necessary to reach out to the network to obtain the necessary information directly. If the necessary information is not provided, the engagement partner would need to consider the implications for managing quality at the engagement level, and determine what additional actions are necessary in the circumstances.

D. Activities Performed by the Network: Group Audit Situations

31. ISA 600 deals with the special considerations that apply to group audits, in particular those that involve component auditors. ISA 220 applies to all audit engagements, and therefore in a group audit situation the requirements of ISA 220 will need to be considered for the engagement as explained

above. It is assumed that the proposed strengthened communication requirements would facilitate the improved flow of information down to the group engagement teams and component auditors involved in the group audit. Further, as the group engagement team and the group engagement partner obtain the required understanding of the component auditor (e.g., understand their competence and capabilities), they also need to understand the activities performed at network level that are related to the component auditor and relevant to the group engagement. If the network firm of which the group engagement team is a part has not obtained the necessary information from the network about the activities that are performed at network level, and which are likely relevant to the component auditor, the group engagement team would need to proactively seek that information (either through the group engagement team's firm, or directly from the network).

32. The Task Forces have also discussed the possible approaches for obtaining information from a network that may be relevant to the various engagements that the firm performs. For example, as part of its quality management system, the firm could identify what information is needed from the network because of its relevance to multiple engagements performed by the firm involving auditors from other network firms, and establish procedures for gathering such information from the network, evaluating the effectiveness of network level activities and communicating the necessary information to the engagements that need it. In this way, individual engagement teams would not have to directly make inquiries or seek information from the network. When a firm has several group engagement teams using the work of the same component auditor from another network firm, relevant information about that component auditor could be obtained by the firm and communicated to those engagement teams, instead of each individual group engagement team having to make the same inquiries. The Task Forces also noted that in many cases information provided by the network firm or the network would have to be supplemented by additional inquiries, observations and other procedures at the engagement level. It is the Task Forces' view that developing robust application material to explain this process would be helpful in encouraging firms to obtain information in the most effective and efficient way. However, the revisions to the IAASB's International Standards should not be too prescriptive with respect to the nature and extent of information that has to be obtained from the networks, or the manner in which it should be obtained.

E. Further Considerations by the Task Forces for Improving the IAASB's standards

33. The Task Forces are of the view that the proposed strengthening of the requirements in ISQC 1 and in ISA 220 related to communication (see **Agenda Item 2-A** and **Agenda Item 5-A**) should also address communications between networks and firms, and where applicable or necessary, between engagement partners or engagement teams and networks. The Task Forces also have the view that application material describing various activities which are typically performed by networks could be developed, including illustrations of what the firm or an engagement team might be expected to do to demonstrate that they are more proactively considering the network activities and the information provided by networks about their effectiveness.

34. Further consideration will need to be given regarding documentation requirements, including the expected level of documentation relating to how a network firm or an engagement team can demonstrate the basis for decisions made about the appropriateness of incorporating network activities into responses for managing quality at either the network firm or the engagement level.

35. In developing the changes to ISQC 1, ISA 220 and ISA 600, the interaction between the standards has been highlighted. ISQC 1 forms the foundation for quality management, with further consideration

about how to embed the concept of managing quality at the engagement level by the engagement partner in ISA 220. In ISA 600, aspects of an audit that are particular to a group audit situation are further considered, in addition to the requirements of ISQC 1 and all the ISAs, including ISA 220. Accordingly, the overarching requirements regarding using network level activities would be established in ISQC 1, with further consideration at the engagement level in ISA 220. ISA 600 would then 'build' on those standards for the aspects that would be particular to group audit situations, likely through application material that would provide further guidance for those specific aspects (e.g., evaluating the competence of component auditors). In addition, the application material could help distinguish the considerations of the group engagement team when using the work of a component auditor that is part of the network and when it operates outside of a network.

Matters for IAASB Consideration:

1. Does the IAASB agree with the overall direction being contemplated by the Task Forces i.e., to strengthen and enhance the requirements and application material in ISQC 1, ISA 220 and ISA 600, and require more proactive consideration or evaluation by network firms, and at the engagement level, before "relying" on network-level quality management activities (for example, a common methodology and tools, monitoring conducted at a network level and related communications)?
   (a) What is the IAASB's view about the work effort that would be necessary to demonstrate the basis for appropriate reliance at the firm and the engagement level? Would the necessary work effort vary depending on what is being relied upon? What are the documentation considerations?
   (b) What are the practical implications of strengthening the requirements as proposed? What challenges would be likely to arise?
   (c) Are there other aspects relating to networks that need to be addressed and/or strengthened in the IAASB's International Standards?
2. Does the IAASB agree with the Task Forces' view that, at this time, no further consideration be given to the definition of "network"?

Appendix A

ITC Sections Addressing Networks

The Firm's Role in Supporting Audit Quality

105. In the current evolving environment, firms are operating in many and varied ways that potentially affect the way that firms and engagement teams are structured and how audits are performed. We believe it is necessary to give further consideration to issues arising in relation to these matters, including:

    (a) Firms that operate through arrangements that share:

        (i) Common policies and procedures for performing the work (e.g., audit methodologies);

        (ii) Common quality control policies and procedures; or

        (iii) Common monitoring policies and procedures.[8]

    (b) Models with service delivery that are different to traditional engagement team structures. These are sometimes referred to as "audit firm shared service centers," "centers of excellence," "on-shoring," "offshoring," or "outsourcing" (referred to in this ITC as ADMs).

Quality Control Considerations When Operating as Part of a Network

106. ISQC 1 refers to the fact that some firms operate as part of a network of firms. The definition of a network in ISQC 1 contains elements that are broader than the sharing of common quality control policies and procedures and common methodologies. In reality, networks of firms vary significantly and the extent of sharing of and reliance on common quality control policies and procedures and common methodologies can vary considerably. For purposes of this ITC, the term "network of firms" (network) refers only to arrangements where firms share common quality control policies and procedures or common methodologies. The following are often observed in network arrangements:

    - Firms within a network are not owned or controlled by the network entity for various reasons, including jurisdictional law and regulation, and risk and litigation management purposes.
    - The extent of operational and decision-making power at the network level varies among networks and enforcement powers in relation to individual network member firms may be limited. Compliance at the individual member firm-level with shared common quality control and monitoring policies and procedures and common methodologies can be influenced through economic and other measures, but often cannot be centrally controlled.

107. Currently very few jurisdictions have law or regulation that govern networks and the way they are structured and managed. Where such law or regulation exists, application is generally limited to firms that operate within the jurisdiction. We acknowledge that firms may be organized under many different arrangements, and recognize that our standards cannot mandate or anticipate all the ways in which firms might be structured today or in the future.

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[8] Firms that operate through such arrangements are typically referred to as a network or network firms. Our standards define a "network" as "A larger structure that is (a) aimed at cooperation; and (b) is clearly aimed at profit or cost-sharing or shares common ownership, control or management, common quality control policies and procedures, common business strategy, the use of a common brand name, or a significant part of professional resources".

108. ISQC 1 and the ISAs do not establish any requirements for firms at the network level nor do they address in any significant detail a firm's ability to place reliance on network policies and procedures to address firm-level or engagement-level responsibilities for quality control.

109. A firm that operates as part of a network may seek to rely on the network's system of quality control (including monitoring policies and procedures), to address some of the firm's responsibilities established by ISQC 1. In relation to this, concerns have been raised by regulators and audit oversight bodies that there may be undue reliance by firms on the network's system of quality control in some circumstances.

110. More specifically, regulators and audit oversight bodies have:

- Highlighted that ISQC 1 does not extend to, or address, the monitoring procedures that may, or may not be, performed at the network level.
- Expressed concerns that networks are not adequately considering the results of external inspection findings of individual firms within the network, and their implications to the network as a whole, and making appropriate communications about such matters within the network.
- Noted concerns about their ability to access audit documentation of other firms in the network, including the ability of firms within the network to share information with them.

111. At the engagement level, issues have arisen about whether, how and under what circumstances engagement teams can rely on the common systems of quality control when using work performed by other auditors from the same firm or a network firm. Specifically, concern has been raised about a group engagement team placing reliance on the firm or network quality control policies and procedures without due consideration of an appropriate basis for doing so. For example, we have heard concerns about situations when a group engagement team may place reliance without conducting a proper assessment on network- level policies and procedures relating to independence, and competence and capabilities of the component auditor (i.e., because the component auditor is believed to have or be subject to the same quality control policies and procedures as the group engagement team).

References to Existing Requirements and Application Material

112. Where firms are within a network that operates under common monitoring policies and procedures, and the firms have implemented monitoring procedures on a network basis that are relied on by the individual firms, ISQC 1 requires firm policies and procedures for communication by the network:

- At least annually, of the overall scope, extent and results of monitoring process to the firms within the network; and
- Of any deficiencies in the system of quality control to the firms in the network so the necessary action can be taken.[9]

113. ISA 600 sets out application material relating to considerations about how the group engagement team's procedures may be affected by whether the group engagement team and component auditor have common policies and procedures for performing the work, common quality control policies and

[9] ISQC 1, paragraph 54

procedures or common monitoring policies and procedures.[10] ISA 220 provides for the ability of the engagement team to rely on the firm's system of quality control, unless information provided by the firm or other parties suggest otherwise.[11] This may include, for example, competence of personnel, independence, maintenance of acceptance and continuance systems, and adherence to applicable legal and regulatory requirements through the monitoring process.[12]

Possible Actions to Address the Issues

114. Clarity in ISQC 1 and ISA 220 about what should be considered and documented by the individual firm as a basis for the reliance on network policies and procedures at the firm level (including for example, a common audit methodology or audit technology) is important. While recognizing the importance of maintaining principles-based standards, specific actions we could take include:

    (a) Revisiting the existing requirements and application material in ISQC 1 to more explicitly address the considerations about the extent to which firms can rely on network quality control and monitoring policies and procedures in designing policies and procedures to comply with ISQC 1 at the firm level. This could include, for example, more clearly describing what the firm is required to do at the firm level, and the engagement level, to appropriately rely on network firm quality control and monitoring policies and procedures. Such revised requirements would need to address what would be expected if the component auditor did not share common quality control and monitoring policies and procedures. We may need to explore alternatives that have similarities to the "service organization" concept followed by corporate entities that choose to rely on others for certain aspects of their financial reporting obligations and the related reporting by service auditors (i.e., using the principles of ISA 402[13] and ISAE 3402).[14]

    (b) Strengthening the requirements and application material in ISQC 1 in relation to inspections that have taken place across the network and related communications, including, for example, providing more specificity about:

        (i) The impact on the firm, and for an engagement, if applicable, of the outcome of these inspections, addressing circumstances where law or regulation may preclude the sharing of information.

        (ii) How the firm responds to the inspection findings.

        (iii) The impact on the firm's own system of quality control, including monitoring policies and procedures, designed to comply with ISQC 1.

115. Paragraph 242(c) sets out possible actions to address issues in a group audit relating to reliance at the engagement level on common systems of quality control and monitoring when using work performed by component auditors from the same firm or a network firm.

116. In exploring possible changes to the standards in relation to network firms, we have recognized that network and firm structures may be highly influenced by law or regulation in the various jurisdictions

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[10] ISA 600, paragraphs A33–A34

[11] ISA 220, paragraph 4

[12] ISA 220, paragraph A2

[13] ISA 402, *Audit Considerations Relating to an Entity Using a Service Organization*

[14] International Standard on Assurance Engagements (ISAE) 3402, *Assurance Reports on Controls at a Service Organization*

where networks and individual firms are established. Mixed views have been expressed about whether requirements for networks themselves could or should be established. We believe it would likely be very challenging for us to develop requirements for networks because:

- Networks or alliances may be structured differently.
- The nature and extent of their common policies and procedures will vary.
- Structures may be highly influenced by applicable law or regulation in the various jurisdictions in which networks and individual firms are established.

We would therefore like to understand stakeholder views on this matter to be able to determine a way forward.

Issues Relating to the Group Engagement Team's Involvement in the Work of the Component Auditors[15]

235. In finalizing ISA 600 as part of our clarity project, we agreed that the requirement for the group engagement team to be involved in the work of the component auditor should be retained, but allowed flexibility for the group engagement team to determine the appropriate nature, timing and extent of such involvement based on the circumstances. In addition, we considered whether to mandate a minimum quantitative threshold for the involvement of the group engagement team in the group audit, but agreed that this would conflict with the risk-based nature of the standard.

236. As discussed in paragraph 70, the group engagement partner takes responsibility for direction, supervision and performance of the group audit engagement.[16] When component auditors perform work on the financial information of components, and the group engagement team will use this work when obtaining evidence on which to base the group audit opinion, the ISA requires that the group engagement team be involved in the audit work of the component auditors to the extent necessary to obtain sufficient appropriate audit evidence.

237. The group engagement team's involvement in the work of the component auditors depends on a number of interrelated factors and judgments, such as the competence and capability of the component auditor, the expected communications between the group engagement team and the component auditors, the identification of significant components and the determination of the necessary work relating to non-significant components. The appropriate nature, timing and extent of the involvement of component auditors will therefore vary according to the circumstances of each group audit engagement (e.g., considering the significance of the components, the significance of the risks of material misstatement related to the components and the results of the understanding of the component auditors), but it must be to the extent necessary to obtain sufficient appropriate audit evidence in order to form the basis for the opinion on the group financial statements.

Issues

238. Some regulators and audit oversight authorities have raised concerns that involvement of the group engagement team in the work of the component auditors is not always adequate, particularly in instances where the group engagement partner is not located where the majority of the audit work is

[15] This section is included because of the relevance of network issues to situations involving component auditors from the same network of firms.

[16] Paragraph 11 of ISA 600

performed. For example, it has been noted in some audit inspection reports that the nature and extent to which the group engagement team specifies or communicates risks of material misstatement, or expected responses, to component auditors varies, resulting in different levels of understanding and potentially different responses. Additionally, ISA 600 does not include guidance about how to deal with situations in which the group engagement team is also performing work at the component level.

239. In addition, certain audit inspection reports have noted that the judgments around the nature, timing and extent of the group engagement team's involvement in the work performed by component auditors, and the reasons therefore, are not always clearly demonstrated (including the documentation by the group engagement team of the relevant considerations supporting its conclusions).

References to Existing Requirements and Application Material

240. The group engagement partner is responsible for the group audit engagement. Where component auditors will perform work on the financial information of components, as part of the acceptance and continuance of the engagement, the group engagement partner is required to evaluate whether the group engagement team will be able to be involved in the work of those component auditors to the extent necessary to determine whether the evidence obtained is sufficient and appropriate in the circumstances and that it will support the conclusions reached.[17]

241. ISA 600 requires the group engagement team to determine the type of work to be performed on the financial information of the components (by the group engagement team or by component auditors on its behalf), and to determine the nature, timing and extent of its involvement in the work of the component auditors.[18] For significant components, there is a requirement for the group engagement team to be involved in the component auditor's risk assessment process to identify significant risks of material misstatement of the group financial statements.[19] ISA 600 specifically requires documentation of the type of work to be performed on the financial information of components,[20] and the nature, timing and extent of the group engagement team's involvement in the work of the component auditors on significant components including, where applicable, the group engagement team's review of relevant parts of the component auditor's audit documentation and conclusions thereon.[21] Guidance about factors[22] that may affect the group engagement team's involvement in the work of the component auditor, as well as examples of forms of involvement, are included in the application material in ISA 600.[23]

Possible Actions to Address the Issues

242. In discussing the responses to address the issues, we identified the following possible actions:

    (a) Strengthening ISA 600 to provide more clarity as to how the group engagement team determines the nature, timing and extent of the necessary involvement in the work of the

[17] ISA 600, paragraph 12

[18] ISA 600, paragraph 24

[19] ISA 600, paragraph 30

[20] ISA 600, paragraph 50(a)

[21] ISA 600, paragraph 50(b)

[22] ISA 600, paragraph A54; see also the connection between A54 (c) and A33.

[23] ISA 600, paragraph A55

component auditors, including more explicit focus on demonstrating why the involvement of the group engagement team is appropriate in light of all relevant considerations and the application of appropriate professional skepticism. However, due to widely varying group structures and variations in component auditors (including as it relates to their competence and expertise), ISA 600 cannot be overly prescriptive in setting forth the nature, timing and extent of appropriate involvement of the group engagement team in the work of component auditors, nor can ISA 600 be expected to address all the different approaches that might be appropriate. For example:

- In some cases, it may be appropriate for a group engagement team to undertake site visits to meet with the component auditors and review their working papers in order to be appropriately involved in their work and effectively evaluate their findings.
- In other circumstances, preparing group instructions and providing them to a component auditor and obtaining a memorandum from the component auditor that describes in sufficient detail the work performed based on the instructions, and the resulting findings and conclusions, may be sufficient for the group engagement team's purposes

(b) Strengthening ISA 600, either through clarification or additions to the requirements or application material, as follows

- Emphasizing the need for greater focus and professional skepticism by the group engagement team on the significant judgments that need to be made about the nature, timing and extent of the involvement of the group engagement team in work performed by the component auditors, and the need for appropriate documentation thereof.[24]
- Clarifying the interrelationships between paragraphs 24, 30, A33, A47 and A54 of ISA 600, to assist auditors in better applying professional judgment in determining the nature, timing and extent of their involvement in the work of the component auditors.
- More explicitly explaining the interactions between the group engagement team and the component auditors in varying circumstances (e.g., in different group structures or in jurisdictions where restrictions on access exist).

(c) Providing further examples in the application material to illustrate the wide variety of circumstances that may affect the determination of the necessary nature, timing and extent of the group engagement team's involvement in the work of the component auditor. Additional examples may help distinguish the varying levels of involvement of the group engagement team that may be appropriate in different circumstances. These examples may address situations where:

- The component auditors and group engagement team are not subject to common policies and procedures.
- The component auditors are from different jurisdictions, or are subject to dissimilar laws or regulations.
- The professional oversight; discipline and external quality assurance; education and training; and professional organizations and standards differ between the component

[24] Paragraphs 8(c) and A8 of ISA 230, *Audit Documentation*, set out the documentation requirements for the significant professional judgments of the auditor in reaching their conclusions

auditor and the group engagement team.

- The language and culture of the component auditor are different from the group engagement team.
- The group engagement team also performs work at the component level.

For example, the nature of the group engagement team's involvement in the work performed by the component auditor when they are not subject to the same policies and procedures (or where there are differences in any of the previously mentioned factors) will likely need to be different, and the nature and timing of such involvement may also need to be different. Depending on the circumstances, more detailed instructions and more frequent communications between the group engagement team and component auditors may be necessary as the audit progresses.

Appendix B

Approved IAASB CAG Public Session Minutes – September 2015

The IAASB CAG discussed network-related issues in its September 2015 meeting.[25] Relevant parts from the approved minutes of that meeting are as follows:

SPECIFIC MATTERS RELATED TO QUALITY CONTROL

Ms. French introduced the topic, noting that the focus of the discussion would be on the three matters highlighted in Agenda Item F.1, which were the areas the IAASB had asked the Quality Control Working Group (QCWG) to further consider during its June 2015 discussions. These matters would also be discussed with the IAASB at its September 2015 meeting.

Quality Control Policies and Procedures at the Firm Level when Operating as Part of a Network of Firms

Ms. French noted that the IAASB suggested the QCWG should give further consideration to how the elements contained in ISQC 1, specifically those related to governance, should take into account the fact that some audit firms operate within a network of firms. She explained that audit firms that operate through a network of firms may share, among other things, common quality control policies and procedures and may seek to leverage the network's system of quality control and related policies and procedures in meeting the individual audit firm's responsibilities in accordance with ISQC 1. She explained that regulators and audit oversight bodies have expressed concerns about:

- Overreliance by audit firms on network-level quality control policies and procedures without an appropriate basis for doing so; and
- Inadequate consideration at the network level of the results of internal and external inspection findings of audit firms within the network, and their implications to not only the network as a whole but also the individual audit firms within the network.

Ms. French further explained that audit firms within a network, for various reasons, including jurisdictional law and regulation and risk and litigation management purposes, may not be controlled by the network entity. The extent of operational and decision-making power at the network level may be limited. As a result, she noted that establishing requirements in ISQC 1 relating to how audit firms are structured, including how audit firms may choose to operate through a network of firms, may be difficult or even inappropriate, as involvement in firms' operational matters is outside of the IAASB's mandate. For these reasons, the QCWG is of the view that it would likely not be appropriate to develop requirements within ISQC 1 or a separate "ISQC 1" like standard aimed specifically at the network entity. Rather, the QCWG is of the view that consideration should be given to additional requirements and application material in ISQC 1 for the audit firm to consider in instances where audit firms seek to place reliance on policies and procedures at the network level to meet their own ISQC 1 responsibilities.

[25] The discussion took place before the finalization of the ITC and the feedbacks from CAG Representatives were taken into account in drafting the issues, proposed actions and questions for respondents that were included in the ITC.

The Representatives and Observers commented as follows:

- Mr. Baumann agreed that quality control policies and procedures should be at the firm level, because the responsibility for complying with the requirements of ISQC 1 apply to individual audit firms. He added that those same principles should also apply to any other audit firms that participate in the audit. Mr. Baumann requested additional clarification as to what the QCWG was suggesting related to additional requirements and application material in ISQC 1 and its application to networks. Ms. French explained that the intent was to make the distinction between imposing requirements on the network entity versus the audit firm. If an audit firm intended on leveraging, or is leveraging, policies and procedures at the network level as a means of meeting its responsibilities under ISQC 1, ISQC 1 could include matters that the audit firm would need to consider to be able to have a basis to do so, as well as how the audit firm would be able to demonstrate that the leveraging of network quality control policies and procedures is appropriate. Mr. Baumann noted that these should be requirements in ISQC 1, rather than guidance about matters that the audit firm would need to consider. Ms. Singh agreed with Mr. Baumann.
- Mr. Stewart drew attention to the definition of a network that had been included in Agenda Item F.1, noting his view that the definition is too broad in the context of an audit firm relying on network policies and procedures in order to meet the audit firms' requirements under ISQC 1. Additionally, he added that if an audit firm wishes to rely on network policies and procedures, similar to Mr. Baumann's remarks regarding the need for ISQC 1 to contain requirements in the event an audit firm is relying on network quality control policies and procedures to meet the audit firm's responsibilities under ISQC 1, the audit firm needs to have a basis for being able to do so, and ISQC 1 should have an appropriate level of clarity as to what that basis should be.
- Ms. Molyneux noted that, while the governance community, including those charged with governance, have an interest in audit quality, this will be a difficult area on which to obtain their input. She noted that, while those charged with governance may have insight into how audit firms operate and, if applicable, the network's quality control policies and procedures, those aspects have far less relevance to those charged with governance compared to details about the individual audit that was performed. Ms. Molyneux noted further that, while she recognized that a lot of effort to create quality control policies and procedures at the network level, these were often applied differently in various jurisdictions. Mr. Dalkin noted, in the context of audits of governmental entities, that these challenges often arise as a result of the audit firm not being able to control or tell other audit firms within the network that are involved in the audit what they need to be doing to address, for instance, a specific governmental requirement relevant to the audit being performed. This becomes more problematic when public expectation would be that the systems of quality control are similar given the way firms market themselves as a network. He supported the IAASB considering these matters as part of the quality control project.
- Mr. van der Ende noted that there appears to be confusion between the application of ISQC 1 at network level and individual audit firm level. In light of his view that there is little that can be done centrally in relation to network member firms, Mr. van der Ende was not convinced that additional requirements in ISQC 1 would help in this regard. He also agreed with other comments made relating to stakeholders' expectations of consistent levels of quality control

across firms in a network in circumstances where networks are marketing and communicating as one firm, when in reality this may not be the case. However, he cautioned against IAASB actions in this area as they would be difficult to implement.

Appendix C

Definition of Network

IAASB's International Standards

The IAASB's Standards contain the following definitions of "network" and "network firm" in ISQC 1 and ISA 220:

> Network[26] – A large structure:
>
> (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 control policies and procedures, common business strategy, the use of a common brand name, or a significant part of professional resources.
>
> Network firm[27] – A firm or entity that belongs to a network.

IESBA Code

The IESBA Code definition of "network" or "network firm" are the same as the IAASB definitions noted above. For purposes of the application of the independence requirements of the IESBA Code indicates that firms shall conclude that a network exists when a larger structure has been formed with other firms and entities to enhance their ability to provide professional services and such larger structure possesses certain characteristics.[28] (Please see Appendix D). Such characteristics include whether entities within the structure share:

- common ownership, control or management (achieved by contract or other means),
- common quality control policies and procedures (which are those designed, implemented and monitored across the larger structure), or
- a significant part of professional resources.

European Union – Audit Directive

In the European Union, the Directive 2006/43/EC of the European Parliament and of the Council[29] contains the network definition and independence rules for network firms. The definition of the network is very similar to the ISA definition:

"Network" means the larger structure

- which is aimed at cooperation and to which a statutory auditor or an audit firm belongs; and
- which is clearly aimed at profit- or cost-sharing or shares common ownership, control or management, common quality-control policies and procedures, a common business strategy, the use of a common brand-name or a significant part of professional resources.

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[26] Paragraph 12(l) of ISQC 1

[27] Paragraph 12(k) of ISQC 1

[28] Paragraphs 290.13 to 290.24 of the extant IESBA Code, and paragraphs R400.51-R400.54 of Proposed restructured Code

[29] Directive 2006/43/EC of the European Parliament and of the Council

FoF

The FoF, is an independent association of international networks established to promote consistent and high-quality standards of financial reporting and auditing practices by involving the networks with IFAC's activities in audit and assurance-related areas. Twenty-seven networks at present belong to the FoF. In terms of the definitions in the FoF Constitution, "network" means "a structure comprising network firms as defined in the IESBA Code." The FoF's membership obligations require, with respect to transnational audits, the application of ISAs, ISQC 1 and the IESBA Code amongst any relevant national standards or codes of ethics, and also the conduct of regular globally coordinated internal quality assurance reviews.

PCAOB

The United States Public Company Accounting Oversight Board (PCAOB) auditing standards do not have a definition for network.

PCAOB Auditing Standard (AS) 1205[30] governs situations when part of the audit is performed by other independent auditors. This standard uses the term "another independent auditor which is an associated or correspondent firm," but does not give further guidance in terms of what this means.

Network is not further described in the recent PCAOB consultation on *Proposed Amendments Relating to the Supervision of Audits Involving Other Auditors*, notwithstanding the term is used in the consultation. In the context of obtaining an understanding about the other auditor's knowledge of the relevant PCAOB and United States Securities and Exchange Commission (SEC) requirements, the discussion paper of the proposal says that sources of relevant information about other auditors may differ depending, for example, on whether the lead auditor and other auditors are affiliated with the same network of audit firms.

Further requirements:

- Quality Control Standard of the PCAOB

  Paragraph 6 of Quality Control Standard 20[31] of the PCAOB says that the system of quality control should provide the firm with reasonable assurance that the segments of the firm's engagements performed by its foreign offices or by its domestic or foreign affiliates or correspondents are performed in accordance with professional standards in the United States when such standards are applicable.

- SEC Practice Section ("SECPS") Requirements

  Section 1000.08(n)—Audit Firm Obligations with Respect to the Policies and Procedures of Correspondent Firms and of Other Members of International Firms or International Associations of Firms:

  For SECPS member firms that are members of, correspondents with, or similarly associated with international firms or international associations of firms, seek adoption of policies and procedures by the international organization or individual foreign associated firms that are consistent with the objectives set forth in Appendix K of SECPS §1000.45[32] for SEC registrants.

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30 AS 1205, *Part of the Audit Performed by Other Independent Auditors*

31 QC 20 - System of Quality Control for a CPA Firm's Accounting and Auditing Practice

32 https://pcaobus.org/Standards/QC/Pages/SECPS_1000.08_appendices.aspx

- The SEC Electronic Data Gathering, Analysis and Retrieval Filer manual on Appendix K:

  6810.5 Effective January 1, 2000, AICPA[33] SEC Practice Section ("SECPS") rules established minimum requirements for the review of SEC filings by a designated "filing reviewer" within the independent accountant's U.S. firm or international organization knowledgeable about U.S. Generally Accepted Accounting Principles, U.S. Generally Accepted Auditing Standards, U.S. auditor independence and SEC reporting requirements. Although the SECPS no longer exists, the PCAOB has adopted the requirements of Appendix K, SECPS §1000.45 pursuant to PCAOB Rule 3400T, through its adoption of Interim Quality Control Standard 1000.08(n), which cross references SECPS § 1000.45. Prior to commencing review of initial registration statements, the staff may request confirmation that Appendix K was applied to the filing, as well as the name of the designated filing reviewer that the staff may contact with any questions concerning the application of those policies and procedures to the registration statement. The purpose of the procedure is to ensure that foreign auditors appropriately involve their designated filing reviewer prior to submission of registration statements. The staff will consider deferring the review of a registration statement where the application of the firm's established policies and procedures to that registration statement cannot be confirmed.

[33] American Institute of Certified Public Accountants

Appendix D

IESBA Code of Ethics for Professional Accountants – Networks and Network Firms

290.13 If a firm is deemed to be a network firm, the firm shall be independent of the audit clients of the other firms within the network (unless otherwise stated in this Code). The independence requirements in this section that apply to a network firm apply to any entity, such as a consulting practice or professional law practice, that meets the definition of a network firm irrespective of whether the entity itself meets the definition of a firm.

290.14 To enhance their ability to provide professional services, firms frequently form larger structures with other firms and entities. Whether these larger structures create a network depends on the particular facts and circumstances and does not depend on whether the firms and entities are legally separate and distinct. For example, a larger structure may be aimed only at facilitating the referral of work, which in itself does not meet the criteria necessary to constitute a network. Alternatively, a larger structure might be such that it is aimed at co-operation and the firms share a common brand name, a common system of quality control, or significant professional resources and consequently is deemed to be a network.

290.15 The judgment as to whether the larger structure is a network shall be made in light of whether a reasonable and informed third party would be likely to conclude, weighing all the specific facts and circumstances, that the entities are associated in such a way that a network exists. This judgment shall be applied consistently throughout the network.

290.16 Where the larger structure is aimed at co-operation and it is clearly aimed at profit or cost sharing among the entities within the structure, it is deemed to be a network. However, the sharing of immaterial costs does not in itself create a network. In addition, if the sharing of costs is limited only to those costs related to the development of audit methodologies, manuals, or training courses, this would not in itself create a network. Further, an association between a firm and an otherwise unrelated entity to jointly provide a service or develop a product does not in itself create a network.

290.17 Where the larger structure is aimed at cooperation and the entities within the structure share common ownership, control or management, it is deemed to be a network. This could be achieved by contract or other means.

290.18 Where the larger structure is aimed at co-operation and the entities within the structure share common quality control policies and procedures, it is deemed to be a network. For this purpose, common quality control policies and procedures are those designed, implemented and monitored across the larger structure.

290.19 Where the larger structure is aimed at co-operation and the entities within the structure share a common business strategy, it is deemed to be a network. Sharing a common business strategy involves an agreement by the entities to achieve common strategic objectives. An entity is not deemed to be a network firm merely because it co-operates with another entity solely to respond jointly to a request for a proposal for the provision of a professional service.

290.20 Where the larger structure is aimed at co-operation and the entities within the structure share the use of a common brand name, it is deemed to be a network. A common brand name includes common initials or a common name. A firm is deemed to be using a common brand name if it includes, for example, the common brand name as part of, or along with, its firm name, when a partner of the firm signs an audit report.

290.21 Even though a firm does not belong to a network and does not use a common brand name as part of its firm name, it may give the appearance that it belongs to a network if it makes reference in its stationery or promotional materials to being a member of an association of firms. Accordingly, if care is not taken in how a firm describes such memberships, a perception may be created that the firm belongs to a network.

290.22 If a firm sells a component of its practice, the sales agreement sometimes provides that, for a limited period of time, the component may continue to use the name of the firm, or an element of the name, even though it is no longer connected to the firm. In such circumstances, while the two entities may be practicing under a common name, the facts are such that they do not belong to a larger structure aimed at co-operation and are, therefore, not network firms. Those entities shall determine how to disclose that they are not network firms when presenting themselves to outside parties.

290.23 Where the larger structure is aimed at co-operation and the entities within the structure share a significant part of professional resources, it is deemed to be a network. Professional resources include:

- Common systems that enable firms to exchange information such as client data, billing and time records;
- Partners and staff;
- Technical departments that consult on technical or industry specific issues, transactions or events for assurance engagements;
- Audit methodology or audit manuals; and
- Training courses and facilities.

290.24 The determination of whether the professional resources shared are significant, and therefore the firms are network firms, shall be made based on the relevant facts and circumstances. Where the shared resources are limited to common audit methodology or audit manuals, with no exchange of personnel or client or market information, it is unlikely that the shared resources would be significant. The same applies to a common training endeavor. Where, however, the shared resources involve the exchange of people or information, such as where staff are drawn from a shared pool, or a common technical department is created within the larger structure to provide participating firms with technical advice that the firms are required to follow, a reasonable and informed third party is more likely to conclude that the shared resources are significant.

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Meeting:	IAASB
Meeting Location:	New York, USA
Meeting Date:	June 19–22, 2017

Agenda Item
9

Professional Skepticism

Objectives of Agenda Item

1. To:

   (a) Receive an oral update on the activities of the joint Professional Skepticism Working Group (PSWG) and the IAASB Professional Skepticism Subgroup (the Subgroup)[1] since the March 2017 meeting from the Working Group Chair.

   (b) Obtain the views of the IAASB on the premises, analysis, conclusions and recommendations related to an invariant vs. variable concept of professional skepticism.

   (c) Obtain the Board's approval for publishing the PSWG publication – *Professional Skepticism – Strengthening the Pillars: Observations of the IAASB-IAESB-IESBA Professional Skepticism Working Group.*

Professional Skepticism Working Group

2. The PSWG includes representatives from the IAASB, the International Ethics Standards Board for Accountants (IESBA), and the International Accounting Education Standards Board (IAESB) and is comprised of the following members:

   - Prof. Annette Köhler, WG Chair, IAASB Member (supported by Wolfgang Böhm, IAASB Technical Advisor)
   - Charles E. Landes, IAASB Member
   - Susan Jones, IAASB Technical Advisor
   - Richard Fleck, IESBA Deputy Chair
   - Patricia Mulvaney, IESBA Member
   - Dave Simko, IAESB Member
   - Bernard Agulhas, IAESB Member

3. The IAASB Subgroup comprises Prof. Köhler, Mr. Landes, and Ms. Jones.

[1] Following the March 2016 IAASB Board meeting, a subgroup of the PSWG was formed (IAASB Subgroup or the Subgroup) in order to address specific areas for consideration raised by the Board. The Subgroup consists of the IAASB-related members of the PSWG.

Activities since the Last IAASB Discussion

4. The Subgroup held one physical meeting and one teleconference to further discuss matters related to potential changes to the concept/definition of professional skepticism within the ISAs. These discussions and the issues arising therefrom are summarized in **Agenda Item 9-A**.

5. Minutes of the March 2017 discussion of the IAASB on Professional Skepticism can be found in the Appendix.

PSWG Publication

6. Subsequent to the March 2017 IAASB meeting, the joint PSWG held two teleconferences to share updates of the IAASB, IESBA, and IAESB, as well as to develop the material included in **Agenda Item 9-B**.

7. In answering the stakeholder calls for joint coordination on the topic of professional skepticism among the three SSBs, the PSWG developed a Stakeholder Communication that summarizes the key messages received from respondents to the IAASB's ITC, feedback provided directly to the IESBA on the topic, and respondents to the IAESB's Consultation Paper about professional skepticism. This publication highlights the key observations of the PSWG, actions that the IAASB, IESBA and IAESB have taken, and intend to take, to address issues with respect to professional skepticism, as well as the role for others. The communication is included as **Agenda Item 9-B.**

8. Upon obtaining approval from all three boards in June 2017, the PSWG intends to finalize and publish the document in July 2017.

Actions Requested

9. The IAASB is asked to provide views on the conclusions and recommended actions of the Subgroup in **Agenda Item 9-A** related to the viability of a variable approach to professional skepticism within the ISAs.

10. The IAASB is asked to provide views on whether there would be objections to the release of the Professional Skepticism Joint Stakeholder Publication (see **Agenda Item 9-B)**.

Material Presented

Agenda Item 9-A	Issues and Recommendations
Agenda Item 9-B	Draft Joint Stakeholder Publication – *Strengthening the Pillars of Professional Skepticism: Observations of the IAASB-IAESB-IESBA Professional Skepticism Working Group*

Appendix

Minutes – IAASB March 2017 Meeting[2]

Prof Köhler provided the Board with an oral update on the activities of the joint Professional Skepticism Working Group (PSWG) as well as the IAASB Professional Skepticism Working Group (the IAASB Subgroup) since the December 2016 Board meeting.

JOINT PSWG ACTIVITIES

Prof. Köhler highlighted that the PSWG is in the process of drafting a joint professional skepticism publication that would give prominence to the work of the PSWG, including the actions that have been undertaken by each of the SSBs, as a result of the feedback provided through responses to the Invitation to Comment (ITC)[3] and other consultations of the SSBs. Prof. Schilder summarized the discussion noting that the draft joint professional skepticism publication will be tabled as an agenda item at the next meeting of the Board for discussion.

Prof. Köhler highlighted that the IESBA is currently considering exposure drafts related to professional skepticism that 1) describes the linkage between the fundamental principles and professional skepticism and 2) seeks to clarify the requirement for a professional accountant to exercise professional judgment when applying the conceptual framework. Prof. Schilder summarized the discussion by stating that a decision would be made regarding whether review by the IAASB would be appropriate once additional information has been communicated by IESBA.

IAASB SUBGROUP ACTIVITIES

Prof. Köhler noted that the IAASB Subgroup have begun analyzing potential fundamental issues related to issues raised by respondents to the ITC in relation to, a requirement to seek contradictory evidence, a shift to a more challenging mindset or presumptive doubt, and introducing a concept of levels of professional skepticism as opposed to the current invariant concept.

WAY FORWARD

The PSWG will continue to develop a joint professional skepticism publication to be presented to all three SSBs at their next meetings in June 2017. The IAASB Subgroup will address one or more of the issues described above relate to the concept of professional skepticism within the ISAs at its upcoming meeting on May 9-10, 2017 in Washington DC.

[2] These draft minutes are still subject to IAASB review and may be subject to further change.

[3] Invitation to Comment, Enhancing Audit Quality in the Public Interest, www.iaasb.org/focus-audit-quality

Agenda Item 9-A

Professional Skepticism—Issues and Recommendations

Objective of the Agenda Item

1. To obtain the views of the IAASB on the premises, analysis, conclusions, and recommendations related to an invariant vs. variable concept of professional skepticism.

A. Introduction – Issues of Focus

1. Based on the Issues Paper provided to the IAASB in its September 2016 meeting[1], in the December meeting of the IAASB, Prof. Köhler, the chair of the Joint Professional Skepticism Working Group (PSWG) provided a presentation that included a proposal on the way forward for the IAASB in relation to the exploration of fundamental changes to the concept of professional skepticism.[2] The minutes of the December 2016 meeting of the IAASB in relation to professional skepticism are provided in Appendix A to this Agenda Paper.

2. The IAASB representatives of the PSWG form the PSWG IAASB Subgroup (the Subgroup) and this group focuses on carrying out the actions that directly impact the IAASB and its projects. This paper represents discussions of the Subgroup.

3. In line with the views of the IAASB expressed at its December 2016 meeting, the Subgroup intends to focus the analysis of implications and potential unintended consequences on the following themes:

   - A requirement to seek out contradictory or inconsistent evidence;
   - A shift to a more challenging mindset or presumptive doubt; and
   - Introducing a concept of levels of professional skepticism (see extract from the minutes in Appendix A).

4. Based upon a detailed preliminary analysis of these three themes that was prepared for the Subgroup and originally formed the basis for Section F of the Issues Paper for the September meeting of the IAASB,[3] the Subgroup has concluded that these three themes are interlinked. Furthermore, these themes are conceptually challenging. For these reasons, the Subgroup believes that as a first step the Subgroup would seek to provide an analysis to the IAASB for further discussion of the central issue: whether an invariant or variable concept of professional skepticism ("levels of professional skepticism") is appropriate. The resolution of this theme would also have an impact on how the other two themes ought to be analyzed thereafter.

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[1] Agenda Item 8-A "Professional Skepticism – Issues (Including Feedback to the ITC) and Joint Working Group's Preliminary Recommendations on the Proposed Way Forward", September 2016 meeting of the IAASB. https://www.iaasb.org/meetings/hong-kong-0

[2] Agenda Item 5-A "Professional Skepticism Presentation", December 2016 meeting of the IAASB. https://www.iaasb.org/meetings/new-york-usa-14

[3] Agenda Item 8-A "Professional Skepticism – Issues (Including Feedback to the ITC) and Joint Working Group's Preliminary Recommendations on the Proposed Way Forward", September 2016 meeting of the IAASB. https://www.iaasb.org/meetings/hong-kong-0

B. Premises Upon Which This Analysis Is Based

5. An understanding of the concept of professional skepticism as currently defined in IAASB engagement standards forms an important part of the basis for considering the implications and related advantages and disadvantages of an invariant versus a variable concept, and for whether consideration ought to be given to changing the current concept. There are a number of **premises** upon which the analysis is based that might be considered as being generally accepted by some IAASB Board members, but questioned by other Board members or by others who read the IAASB publicly available Agenda Papers. For these reasons, the Subgroup has chosen to make these premises explicit before providing the analysis of the implications and related advantages and disadvantages of an invariant versus a variable concept of professional skepticism. The analyses supporting each of these premises are provided in Appendices to this Agenda Paper. This approach has the advantage of permitting those who regard these premises as being generally accepted to not need to read the material supporting the premises, while providing the additional analyses for those readers who may wish to refer to them.

5. Appendix B to this Agenda Paper provides an analysis of how the concept of professional skepticism, as currently defined, compares with other related defined and undefined concepts in the ISAs. Based on the analysis in Appendix B to this Agenda Paper, "professional skepticism" in IAASB engagement standards for assurance engagements represents a "term of art" for a concept that is defined as an attitude that involves:

- Exercising a questioning mind,
- Being alert to conditions that may indicate possible misstatements, and
- Critically assessing evidence.

6. Although the concept of professional skepticism is used to evaluate whether sufficient appropriate audit evidence has been obtained, and therefore whether audit risk has been reduced to an acceptably low level and consequently reasonable assurance has be obtained, the concept can be clearly distinguished from these and other related concepts in the ISAs. In particular, professional skepticism plays an important role in considering the persuasiveness of audit evidence.

Premise 1

The concept of professional skepticism as currently defined can be clearly distinguished from other related concepts in the ISAs and plays an important role in considering the persuasiveness of audit evidence.

7. Appendix C to this Agenda Paper provides an analysis of how the concept of professional skepticism as currently defined compares with a number of concepts in the IESBA Code of Ethics (hereinafter referred to as the "Code") that may be related to the meaning of professional skepticism or that refer to professional skepticism. These concepts in the Code comprise the fundamental principles of the Code and two concepts of independence.

8. Based upon the analysis in Appendix C to this Agenda Paper, the concept of professional skepticism extends beyond the concepts in the Code because it involves a questioning mind, being alert to conditions which may indicate possible misstatement, and a critical assessment of evidence – none of which are covered in the fundamental principles or independence as defined in the Code, but are important for the performance of assurance engagements. Consequently, even though the responses

to the IAASB's Invitation to Comment (ITC)[4] suggest that the inappropriate application of professional skepticism might actually be indicative of inappropriate application of the fundamental principles of the Code or independence of mind, the concept of professional skepticism applicable to assurance engagements is separate from the concepts in the Code.

Premise 2

Although the responses from the ITC suggest that the inappropriate application of professional skepticism might be indicative of inappropriate application of the fundamental principles or of independence of mind as defined in the IESBA Code of Ethics, the concept of professional skepticism as currently defined in IAASB engagements standards applicable to assurance engagements extends beyond the fundamental principles and independence as currently defined in the Code.

9. Appendix D to this Agenda Paper provides an analysis of how the concept of professional skepticism as currently defined compares with the concept of "skepticism" as commonly defined and understood.

10. On this basis of the analysis in Appendix D to this Agenda Paper, it can be argued that skepticism as commonly understood involves the disposition to need information (evidence) about the credibility of other information before drawing a conclusion on that credibility.

11. In addition, the meaning of the term "professional skepticism" is NOT the combination of literal meaning of the adjective "professional" and of the noun "skepticism" as commonly defined and understood. Consequently, the term "professional skepticism" as currently defined does not mean "skepticism exercised by a professional (or professional accountant)", but rather means exercising a questioning mind, being alert to conditions that may indicate possible misstatements, and critically assessing evidence, in an assurance engagement.

12. What sets professional skepticism apart from skepticism as commonly defined is the 1. alertness to the sources of potential misstatements and 2. critical evaluation of whether evidence is as persuasive as it needs to be. The former provides a basis for the application of a questioning mind about the credibility of the contents of the financial statements and helps drive the nature and extent of the evidence obtained (through risk assessment procedures and responses to assessed risks) needed to satisfy the auditor. The result of the latter (the critical evaluation) prompts an auditor to obtain additional evidence when the auditor concludes that the evidence is not as persuasive as it needs to be.

13. These points are central to what an assurance engagement is all about: alertness to, and consideration or assessment of, risks of material misstatement, and the need to seek to obtain evidence until the assurance practitioner concludes that the evidence obtained is persuasive enough. For these reasons, professional skepticism as currently defined in IAASB Standards is a crucial additional aspect of assurance engagements beyond skepticism as commonly defined.

[4] ITC, *Enhancing Audit Quality in the Public Interest: A Focus on Professional Skepticism, Quality Control and Group Audits*. *http://www.ifac.org/publications-resources/invitation-comment-enhancing-audit-quality-public-interest*

Premise 3a

Skepticism as commonly defined and understood involves the disposition to question and need information (evidence) about the credibility of other information before drawing a conclusion on that credibility.

Premise 3b

Professional skepticism goes beyond skepticism as commonly defined in that professional skepticism requires

1. Alertness to the sources of potential misstatements, and
2. A critical evaluation of whether evidence is as persuasive as it needs to be.

Premise 3c

The two matters in Premise 3b for which professional skepticism goes beyond skepticism as commonly defined are of central importance to assurance engagements.

Matter for IAASB Consideration

1. Does the IAASB agree with the premises underlying the analysis of the implications and related advantages and disadvantages of an invariant versus a variable concept of professional skepticism? Why or why not?

C. Analysis of an Invariant vs. Variable ("levels") Concept of Professional Skepticism

The Current Invariant Concept in IAASB Engagement Standards

14. Currently, the ISAs and IAASB assurance standards (Paragraph 15 of ISA 200,[5] paragraph 22 of ISRE 2400,[6] and paragraph 37 of ISAE 3000[7] (Revised)) require the auditor to exercise professional skepticism without applying different "levels" of professional skepticism – that is, professional skepticism is an invariant concept. This is partly because in finalizing the ISAE 3000 and ISRE 2400 projects, the IAASB decided that professional skepticism does not vary by level of assurance (that is, the "level" is the same for limited and reasonable assurance). The use of an invariant concept of professional skepticism is in line with how professional skepticism is currently being used in auditing standards in other major jurisdictions.

15. In line with this policy, the ISAs neither use the term "levels of professional skepticism", nor does the wording in the ISAs imply that such levels exist. There is one exception in ISA 240[8] paragraph A33 in relation to fraud, in which this paragraph speaks of "increased professional skepticism" regarding the overall conduct of the audit in relation to fraud. This was a conscious decision of the IAASB at the time because risks of fraud are a special case where for example, as part of overall responses to

[5] ISA 200, *Overall Objectives of the Independent Auditor and the Conduct of an Audit in Accordance with International Standards on Auditing*

[6] ISRE 2400, *Engagements To Review Financial Statements*

[7] ISAE 3000 (Revised), *Assurance Engagements Other than Audits or Reviews of Historical Financial Information*

[8] ISA 240, *The Auditor's Responsibilities Relating to Fraud in an Audit of Financial Statements*

assessed risks of material misstatement due to fraud, forensic experts may be used that would apply completely different notions of skepticism and evidence.[9] The question arises whether this exception implies that there are in fact different "levels" of "professional skepticism", or whether this exception is actually inconsistent with the invariant approach and that therefore this exception ought to be amended. The examples of additional actions prompted by the exercise of professional skepticism in paragraph A33 suggest that it is the actions that are variable and that hence the latter view is correct, rather than the former view of a variable exercise of professional skepticism. This seems to be in line with how the ISAs deal with professional skepticism as described further in paragraphs 16 to 18 below.

16. An invariant concept of professional skepticism implies that the exercise of professional skepticism by auditors does not vary in the circumstances when making professional judgments about the nature, timing and extent of procedures that auditors perform, but that the actual nature, timing and extent of procedures, that auditors judge are necessary given their exercise professional skepticism, would need to vary in the circumstances – i.e., the actions that auditors undertake are context-specific. For example, audit procedures with respect to accounting estimates differ from audit procedures with respect to cash receipts. In this circumstance, the extent to which the exercise of professional skepticism leads to the acceptance or rejection of evidence as being persuasive enough depends upon the context.

17. The ITC provided a simplified paradigm for the application of professional skepticism in a diagram by positing that auditors exercise the attitude of professional skepticism when making professional judgments, and that these judgments prompt actions by the auditor that are then documented.[10] This paradigm implies that, even if the attitude of professional skepticism does not vary, the judgments made and the actions prompted by these do vary in the circumstances – that is, the "levels" needed to deal with different circumstances are embodied in the professional judgments made and actions taken, rather than in the attitude of professional skepticism itself. In other words, professional skepticism causes auditors to adjust their judgments and actions based upon what auditors believe "can go wrong".

18. Examples of how the ISAs currently address the use of context-specific actions that would result from the exercise of professional skepticism in applying professional judgments include:

    - ISA 240, paragraph A17, in which an auditor's exercise of professional skepticism may cause the auditor to judge it necessary to corroborate responses to inquiries with other information;
    - ISA 300,[11] paragraph A3, in which an auditor exercises care in discussing audit procedures with management as part of audit planning so as to not make audit procedures too predictable;
    - ISA 315 (Revised),[12] paragraph 10, in which the nature, timing and extent of the discussion of

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[9] For a more detailed treatment of the treatment of professional skepticism in IAASB Standards, see Agenda Item 8-D "Supplemental Reference Material – for IAASB Information; Background Information Paper: Current Treatment of the Concept of Professional Skepticism in IAASB and IAESB Standards, the IESBA Code, and the IAASB ITC on Audit Quality", from the IAASB meeting in September 2016.

[10] IAASB, Invitation to Comment: Enhancing Audit Quality in the Public Interest – A Focus on Professional Skepticism, Quality Control and Group Audits, p. 13.

[11] ISA 300, *Planning An Audit of Financial Statements*

[12] ISA 315 (Revised), *Identifying and Assessing the Risks of Material Misstatement through Understanding the Entity and Its Environment*

the engagement partner and other key engagement team members in relation to the susceptibility of the entity's financial statements to material misstatement will depend upon the exercise of professional skepticism by being alert to conditions that may indicate possible misstatement due to fraud or error;

- ISA 330,[13] paragraph 5, in which the nature, timing and extent of overall responses to address assessed risks of material misstatement at the financial statement level will vary depending upon the auditor's judgements using professional skepticism about these assessed risks; and
- ISA 500,[14] paragraph 11, in which the auditor needs to determine modifications or additions to audit procedures when evidence from one source is inconsistent with that from another or the auditor has doubts about the reliability of information to be used as audit evidence.

19. The main potential issues with the continued use of an invariant concept of professional skepticism appear to be:

- It appears counterintuitive to those who may not be aware of the meaning of the current definition of "professional skepticism" as a "term of art" and may therefore be basing their views on the concept of "skepticism" as commonly defined (the disposition question and to need evidence about the credibility of information before drawing a conclusion on that credibility) and consequently believe that one needs to be more skeptical (i.e., have a greater such disposition) in some circumstances than others;
- It is inconsistent with the variable approach currently used in most academic literature on professional skepticism; and
- It is inconsistent with the views of those who believe that the concept of professional skepticism ought to represent a continuum of sorts that differentiates among a "presumption of good faith", a "neutral mindset", a "questioning mindset", a "challenging mindset" and "presumptive doubt" (it is actually unclear where a "questioning mindset", a "challenging mindset" and "presumptive doubt" might be placed relative to one another on such a continuum) – this issue will not be dealt with further in this paper, but in a paper, for subsequent IAASB meeting, that builds on the conclusions of this paper.

Matter for IAASB Consideration

2. Does the IAASB agree with the description of the current invariant approach to professional skepticism? Why or why not? Are there any other important issues with the current invariant approach?

Using Levels of Professional Skepticism, Rather Than the Current Invariant Concept

20. Some respondents suggested that the ISAs ought to apply a variable rather than the current invariant approach to the concept of professional skepticism (see Appendix E to this Agenda Paper). A variable approach to professional skepticism implies that it 1. varies and 2. must vary in relation to something – that is, its variation is not a random occurrence. The question of with what professional skepticism ought to vary given a variable concept depends upon the meaning of professional skepticism and

[13] ISA 330, *The Auditor's Responses to Assessed Risks*

[14] ISA 500, *Audit Evidence*

therefore ultimately on what the concept is for (i.e., why the concept is needed in addition to other concepts that already exist in auditing and assurance standards, the Code and the concept of skepticism as commonly defined).

21. The main suggestion set forth by respondents (and found in some academic literature) in relation to with what professional skepticism varies is the risk of material misstatement – in particular, that greater professional skepticism might be required for higher risks of material misstatement. However, this approach appears to be problematic from a conceptual point of view for the following reasons:

- Professional skepticism as a concept was designed to operate on a much broader level than just responses to assessed risk of material misstatement to also cover the basis for risk assessment (the "being alert to conditions which may indicate possible misstatement due to error or fraud" in the current definition). Having professional skepticism vary with the risks of material misstatement appears to limit the application of professional skepticism to responses to risks of material misstatement, which appears to weaken the concept compared to the current definition.
- A greater likelihood of material misstatement simply leads to responses by the auditor to obtain sufficient appropriate audit evidence to reduce that risk to an acceptably low level (i.e., the greater the risk, the more persuasive the evidence required to address that risk needs to be). It is not clear why a separate concept of professional skepticism is needed at all to address the likelihood of occurrence of risks of material misstatement because this is already covered by the responses of the auditor to obtain sufficient appropriate audit evidence to reduce that risk to an acceptably low level.
- Professional skepticism as currently defined is also about the auditor's evaluation of whether the evidence is regarded as sufficient and appropriate (i.e., the "critical assessment of audit evidence" in the current definition). This need to evaluate the persuasiveness of evidence applies regardless of whether more or less persuasive evidence is needed to respond to the risk of material misstatement, even if the work effort involved in evaluating the persuasiveness of the evidence obtained is more likely to be greater for evidence for which it is more difficult to evaluate how persuasive the evidence is. Consequently, the need to evaluate the persuasiveness of audit evidence applies equally regardless of whether a risk of material misstatement is higher or lower. It would therefore be inappropriate to have professional skepticism vary with the risk of material misstatement in this respect.

22. For these reasons, having professional skepticism vary with the risk of material misstatement does not appear to be a fruitful approach for further exploration.

Matter for IAASB Consideration

3. Does the IAASB agree that having professional skepticism vary with the risk of material misstatement does not appear to be worth pursuing further? Why or why not?

23. The question then arises whether it might be useful to have professional skepticism vary with something else, and what the basis for that might be. As noted above, the invariant approach to professional skepticism appears counterintuitive to those who may not aware be of the meaning of the current definition of "professional skepticism" as a "term of art" and may therefore be basing their views on the concept of "skepticism" as commonly defined (the disposition to question and to need

evidence about the credibility of information before drawing a conclusion on that credibility) and consequently believe that one needs to be more skeptical (have a greater such disposition) in some circumstances than others. Seeking to apply a variable approach to professional skepticism on this basis would involve a reconciliation of sorts between skepticism as commonly defined and professional skepticism.

24. A reconciliation between the concepts of skepticism as commonly defined and professional skepticism would not be needed for those parts of the concepts of skepticism and professional skepticism that overlap (respectively: the disposition to question; an attitude that involves a questioning mind). The same applies to that part of the concept of skepticism (to need evidence about the credibility of information before drawing a conclusion on that credibility) essentially covered by the definition of an assurance engagement ("aim to obtain sufficient appropriate evidence in order to express a conclusion designed to enhance the degree of confidence of users … about the subject matter information"[15]).

25. The application of the common meaning of skepticism would mean that the disposition to question and the need for evidence would vary with the evidence needed to allay existing doubts. The consequence of this approach would be to link professional skepticism to the level of assurance sought and therefore to the level of assurance required to be meaningful to users to meet their needs as described in the first bullet point of paragraph A7 in ISAE 3000 (Revised), which refers both to different levels of limited assurance and to reasonable assurance. Consequently, this approach might have the additional benefit of addressing the suggestion by one regulator respondent to seek to link professional skepticism to user needs. This approach may also provide a basis for supporting a higher level of professional skepticism in relation to potential misstatements due to fraud as currently described in ISA 240, in which special approaches (e.g., forensic procedures) might become necessary in some circumstances. Overall, the implication of this approach would be that professional skepticism varies with the level of assurance sought[16] – that is, the level of professional skepticism is clearly linked to decisions about the sufficiency and appropriateness of evidence (its needed persuasiveness) and hence work effort.

26. For this approach to work the two aspects of professional skepticism (being alert to conditions which may indicate possible misstatement, and the critical evaluation of evidence) not covered by either skepticism as commonly defined need to be reconciled into the model by having these also vary with the level of assurance sought. This would imply the following:

    - *For an engagement for which less assurance is sought (e.g. a review of financial statements), the practitioner would be less alert to conditions which may indicate possible misstatement.* For limited assurance engagements, both ISAE 3000 and ISRE 2400 provide for a consideration of risks of material misstatement that is less deep and hence involves less work effort than the risk assessment required for reasonable assurance engagements under ISAE 3000 or audits under the ISAs, respectively. Consequently, one could argue that by doing less

[15] ISAE 3000, paragraph 12 (a).

[16] This would definitely mean that professional skepticism varies between audits and reviews, and between reasonable and limited assurance engagements under ISAE 3000. It would also mean that professional skepticism would vary among different types of limited assurance engagement under ISAE 3000, since different ranges of meaningful levels of limited assurance are contemplated by ISAE 3000. However, this approach could be agnostic as to whether reasonable assurance varies within audits or within the same types of reasonable and limited assurance engagements under ISAE 3000 – i.e., this latter controversial issue need not be explicitly addressed.

work in relation to the consideration of risks of material misstatement, practitioners are effectively being "less alert" for conditions indicating possible misstatement in limited assurance compared to reasonable assurance engagements. One could also seek argue that the threshold for needing to identify such conditions might be less for a limited assurance engagement, since in a limited assurance engagement one is satisfied with evidence of lesser quality (e.g., the results of inquiry and analysis for reviews) than for reasonable assurance engagements. On the other hand, it could be argued that "alertness" is a difficult concept to subject to a sliding scale and that it could be difficult to justify why and how a practitioner is "more alert" in some circumstances than others. In any case, a move towards a sliding scale of "alertness" would involve some exploration of what it would involve and whether that is desirable.

- *For engagements in which less assurance is sought, the practitioner's critical evaluation of the persuasiveness of evidence would involve less work effort.* ISAE 3000, the ISAs and ISRE 2400 require the practitioner to evaluate the sufficiency and appropriateness of evidence obtained, but make no distinctions between the levels of assurance. Furthermore, no distinction is made in these standards in relation to the consideration of the persuasiveness of evidence. Practitioners generally obtain less evidence in a limited assurance engagement than in a reasonable assurance engagement, so at first glance the view that less work effort is involved in evaluating the persuasiveness of evidence for limited assurance engagements than reasonable assurance engagements can appear intuitive. Nevertheless, for given evidence, it may be difficult to argue why the work effort to *consider* its persuasiveness ought to be less for limited vs. reasonable assurance engagements and so why this distinction is needed. On the other hand, if a critical *evaluation* of the persuasiveness of evidence is required, one could argue that the nature and extent of such evaluation might depend upon the nature and extent of the procedures applicable in a particular engagement (e.g., primarily inquiry and analysis in a review, as opposed to other procedures), and hence of the level of assurance. However, this would imply that the underlying concept of assurance would be changed from the converse of engagement risk to the risk that audit risk has not been reduced to an acceptably low level (or conversely, the confidence with which an auditor believes that audit risk has been reduced to an acceptably low level).[17] In any case, this would involve a fundamental change to the current audit risk model paradigm. It is unclear what the benefits and costs of such a paradigm shift might involve.

27. Consequently, seeking to introduce a variable concept of professional skepticism would involve reconsideration of the meaning of reasonable assurance and its link to engagement or audit risk so that the concept of assurance is more closely linked to the risk that sufficient appropriate evidence has not been obtained. This would involve fundamental change to the entire audit model (and the model for all assurance engagements). Given the current concept of assurance (the converse of audit or engagement risk), the difficulties in seeking to apply a variable concept of professional skepticism to those parts of the concept beyond the common meaning of skepticism are not easily surmountable. Changing the meaning of assurance represents a conceptual framework type issue that extends far

[17] This would involve changing the concept of assurance to the "meta-probability" that audit risk has been reduced to an acceptably low level. This approach might have some theoretical appeal because the level of assurance would then be linked to the risk that the appropriate level of a primary aspect of audit quality has not been achieved, as opposed to the risk that the financial statements are materially misstated after the completion of the audit.

beyond the mandate of a project seeking to deal with professional skepticism. While further work on the foundations of assurance engagements might be desirable in the very long run, it is unclear what the benefits would be and there would be few, if any, benefits in the short- to medium-term.

28. Furthermore, it is unclear what the incremental benefits would be of introducing a variable concept of professional skepticism in this way, since the current invariant concept already includes variable professional judgments and variable actions prompted by those judgments.

Matter for IAASB Consideration

4. Does the IAASB agree with the analysis of with what professional skepticism might vary and that this leads to conceptual framework type issues that are beyond the mandate of the project on professional skepticism and that the potential benefits of pursuing the issue are questionable given the variable nature of professional judgements and actions under the extant invariant approach? Why or why not?

C. Conclusion

29. The concept of professional skepticism can be clearly delineated from other related concepts in IAASB engagement standards and from the fundamental principles in the IESBA Code and from the concepts of independence therein. Furthermore, based on the current definition of the concept of professional skepticism, the concept plays a central role in assurance engagements, including audits, beyond the other concepts in IAASB engagement standards and the IESBA Code. The concept of professional skepticism as currently defined in IAASB engagements standards goes beyond the common meaning of the term “skepticism”, even though there are some important overlaps between the definitions of professional skepticism and assurance engagements, on the one hand, and skepticism as commonly defined, on the other hand. What distinguishes professional skepticism from skepticism as commonly defined is the need to:

- Be alert to conditions which may indicate possible misstatement, and
- Perform a critical assessment of evidence.

30. Although there are issues with the continued use of an invariant concept of professional skepticism, it would be very difficult to seek to change the concept to a variable one because of the items in the definition of professional skepticism that go beyond the concept of skepticism that play such an important role in assurance engagements, including audits. It would therefore not be advantageous to seek to weaken the definition of professional skepticism by removing these parts of the definitions or to seek to have them vary. Furthermore, changing to a variable concept of professional skepticism without removing these parts would likely involve fundamental changes to the meaning of assurance, the benefits of which are questionable at this time. For these reasons, the Subgroup believes that pursuing a variable concept of professional skepticism is not in the public interest at this time or in the short to medium-term.

31. For these reasons, the Subgroup recommends that the IAASB not further pursue a variable concept of professional skepticism at this time or in the short to medium-term.

Matter for IAASB Consideration

5. Does the IAASB agree that it is not in the public interest that the variable concept of professional skepticism be pursued at this time or in the short to medium-term? Why or why not? Are there other issues that need to be considered when drawing a conclusion in this matter?

D. Recommendations

32. It should be recognized that that a decision not to further pursue a variable concept of professional skepticism would have implications for the analysis of the other two issues that the Subgroup will focus upon in its further analysis. The Subgroup believes that the analysis of neither of these two issues would have an impact on the analysis in this paper.

33. However, the analysis of the meaning of professional skepticism does indicate that some minor improvements to the definition of professional skepticism might be considered in the public interest, and that better – and in particular, better structured – guidance on the meaning of professional skepticism could be considered. In particular,

- The definition does not specify what about evidence is being critically assessed or evaluated (its persuasiveness), and
- The guidance does not adequately explain how professional skepticism has an impact on
  - Risk assessment;
  - Risk response;
  - The evidence gathered; and
  - The evaluation of the sufficiency and appropriateness of evidence.

These matters could be undertaken by the planned project on audit evidence (together with professional skepticism).

34. The Subgroup also recommends that the IAASB consider whether it would be in the public interest to communicate with its stakeholders soon and in a more effective manner than in the past about the meaning of professional skepticism in current IAASB engagement standards and why it is simply not "skepticism exercised by a professional", but involves matters that go beyond what is commonly understood by the term "skepticism".

Matter for IAASB Consideration

6. Does the IAASB agree with the above recommendations proposed in the public interest? Why or why not? Based on the analysis in this Agenda Paper, are there any other recommendations that the IAASB believes are worthy of consideration?

Appendix A

Excerpt from the Minutes Relating to Professional Skepticism – IAASB December 2016 Meeting

Prof Köhler presented **Agenda Item 5-A** to the Board and provided an update of the activities of the Professional Skepticism Working Group (PSWG) since the September 2016 Board meeting. Prof Kohler highlighted the work streams being pursued by the different Boards, and explained that it is not clear what the IAESB is interested in with the planned literature review, but that she would report back to the Board with this information.

JOINT PSWG ACTIVITIES

Prof. Kohler highlighted that the PSWG will develop a joint Professional Skepticism stakeholder communication that would give prominence to the work, individually and in coordination, that the standard-setting boards (SSBs) will be undertaking in response to the feedback received by all three SSBs. The IAASB asked the PSWG to clarify:

- The purpose of the stakeholder communication and whether it would seek to obtain additional feedback in some way or serve as an "awareness" piece.
- What is meant by "call to action" and to whom it relates.

EXPLORING FUNDAMENTAL CHANGES TO THE CONCEPT OF PROFESSIONAL SKEPTICISM

The following views were expressed about the PSWG's discussion of the potential changes to the concept of professional skepticism within the ISAs:

- Concern with the practicality of "No definition of professional skepticism" as an option being analyzed by the PSWG.
- A shift to presumptive doubt would be challenging, while one Board member commented that in his particular jurisdiction, an auditor is not permitted to accept an engagement if he or she has doubts about management.
- Related to the potential option of extending professional skepticism to all professional accountants (PAs), there was the view that the mindset of an auditor is different from that of a professional accountant and that the auditor's questioning mindset has a clear object, management. But in the case of a professional accountant, who would be the object of their questioning/critical mindset?

The IAASB representatives of the PSWG will focus the analysis of implications and unintended consequences of the following options: 1) A requirement to seek out contradictory evidence, 2) a shift to a more challenging mindset or presumptive doubt, and 3) introducing a concept of levels of professional skepticism.

IESBA SHORT-TERM PROPOSED LANGUAGE

Mr. Richard Fleck (IESBA Deputy Chair and PSWG member) provided the Board with an update regarding the short-term proposals to be considered by the IESBA at its meeting the following week from December 12th–16th. The Board provided the following feedback to the IESBA representatives:

- Support for the proposal to clarify the linkage between professional skepticism and the fundamental principles/independence through additional application material in the IESBA Code of Ethics.
- In relation to the proposed text related to "critical mindset":

- It was not clear what problem the proposals regarding a "critical mindset" are attempting to fix.
- It was noted that the use of the word "mindset" makes a very close link to the "questioning mind" wording in the definition of professional skepticism within the ISAs and instead suggested alternative terms such as "critical thinking."
- Given that the term "critical mindset" is a new concept, it is difficult to foresee how it will change auditor behavior, especially for professional accountants in business. It was also noted that there was a risk of unintended consequences.

Prof. Schilder thanked Mr. Fleck for taking steps to be responsive to the feedback provided to him by the IAASB at its September meeting. He summarized the feedback from the board in two ways:

- Generally, the Board members felt the concept was interesting, but struggled to understand what is meant, and expected, by the concept of "critical mindset"; and
- Board members questioned how this concept is different from professional skepticism and how the two terms would be reconciled.

Prof. Schilder closed the session by requesting that Mr. Fleck ask the IESBA to consider sharing a fatal-flaw review of the exposure draft with the full PSWG following the IESBA meeting, prior to its finalization. Mr. Fleck agreed to ask the IESBA to consider this.

WAY FORWARD

The PSWG intends to continue to progress the stakeholder communication publication and update the Board at future meetings.

Appendix B

For Premise 1: Comparison and Analysis of Concept of Professional Skepticism to Other Related Terms in the ISAs

1. There are a number of fundamental terms used in the ISAs for which the concepts represented by those terms appear to have some relationship to the concept of professional skepticism. Some of these terms are defined – others are not. The defined and undefined terms comprise:

   - Audit evidence (and in particular, the undefined term "sufficient appropriate audit evidence")
   - Audit risk
   - Professional judgment
   - Reasonable assurance
   - The persuasiveness of audit evidence or "persuasive audit evidence"

2. The definitions of the defined terms in ISA 200, including of professional skepticism, are as follows:[18]

> **Audit evidence**
>
> Information used by the auditor in arriving at the conclusions on which the auditor's opinion is based. Audit evidence includes both information contained in the accounting records underlying the financial statements and other information. For purposes of the ISAs:
>
> (i) Sufficiency of audit evidence is the measure of the quantity of audit evidence. The quantity of the audit evidence needed is affected by the auditor's assessment of the risks of material misstatement and also by the quality of such audit evidence.
>
> (ii) Appropriateness of audit evidence is the measure of the quality of audit evidence; that is, its relevance and its reliability in providing support for the conclusions on which the auditor's opinion is based.
>
> **Audit risk**
>
> The risk that the auditor expresses an inappropriate audit opinion when the financial statements are materially misstated. Audit risk is a function of the risks of material misstatement and detection risk.
>
> **Professional judgment**
>
> The application of relevant training, knowledge and experience, within the context provided by auditing, accounting and ethical standards, in making informed decisions about the courses of action that are appropriate in the circumstances of the audit engagement.
>
> **Professional skepticism**
>
> An attitude that includes a questioning mind, being alert to conditions which may indicate possible misstatement due to error or fraud, and a critical assessment of audit evidence.

[18] ISA 200, paragraph 12.

Reasonable assurance

In the context of an audit of financial statements, a high, but not absolute, level of assurance.

3. The current definitions in the ISAs of professional judgment and professional skepticism indicate that these two concepts are quite different, which is in line with the description of the concepts in paragraphs 24 to 27 of the ITC issued by the IAASB in December 2015. Paragraph 17 of ISA 200 provides an indication of the relationship between 3 of the terms above (sufficient appropriate audit evidence, audit risk and reasonable assurance) by using the following wording:

   "To obtain *reasonable assurance*, the auditor shall obtain *sufficient appropriate audit evidence* to reduce *audit risk to an acceptably low level*…".

4. While this requirement does not equate these terms, it does suggest that audit risk has been reduced to an acceptably low level when sufficient appropriate audit evidence has been obtained, and that reasonable assurance has been obtained when audit risk has been reduced to an acceptably low level. As paragraph 4 of Agenda Item 6-A "ISAE 3000 Assurance Engagements other than Audits or Reviews of Financial Statements—Issues and IAASB Task Force Proposals" from the September 2010 IAASB meeting on the revision of ISAE 3000 notes (and with which the subsequent minutes do not indicate that the IAASB disagreed):

   "…the level of assurance obtained is the converse of the reduction in engagement risk, and both of these are an expression of the strength (the combination of sufficiency and appropriateness) of the evidence obtained. Hence, assurance, risk, and evidence are just different perspectives of the same issue."

5. In this context, a review of the term "persuasiveness of audit evidence" or "persuasive audit evidence" as used throughout the ISAs appears to indicate that the "persuasiveness" of audit evidence refers to the strength (the combination of sufficiency and appropriateness) of the evidence described above.

6. The current definition of professional skepticism defines the concept as **an attitude that includes** the following:

   - A questioning mind,
   - Being alert to conditions which may indicate possible misstatement due to error or fraud, and
   - A critical assessment of audit evidence.

7. On this basis, professional skepticism is not the same as reasonable assurance, the sufficiency and appropriateness or persuasiveness of evidence, or an acceptably low level of audit risk. Rather, based on the current definition, and in particular the reference therein to being alert to conditions which may indicate possible misstatement due to error or fraud, it appears that professional skepticism is an attitude that is exercised in order to enable the auditor to obtain reasonable assurance and sufficient appropriate audit evidence, and reduce audit risk to an acceptably low level. Furthermore, based on the reference in the definition to "a critical assessment of audit evidence", it could be argued that professional skepticism is used to evaluate whether sufficient appropriate audit evidence has been obtained, and therefore whether audit risk has been reduced to an acceptably low level and consequently reasonable assurance has be obtained. At a more granular level, this would imply that professional skepticism has an important role to play in considering the persuasiveness of audit evidence.

8. The IAASB engagement standards only use the concept of professional skepticism in the IAASB standards applicable to audits, reviews and other assurance – not in the IAASB standards applicable to related services (compilation engagements and agreed-upon procedures engagements). This treatment of professional skepticism within IAASB engagement standards (that is, the restriction of the use of the concept to only assurance engagements) is therefore consistent with the definition of professional skepticism, which relates only to engagements that involve both misstatements and evidence as defined in those standards – i.e., assurance engagements.[19]

9. In conclusion, professional skepticism as used in IAASB engagement standards for assurance engagements represents a "term of art", and the concept of professional skepticism is an attitude that involves:

   - Exercising a questioning mind,
   - Being alert to conditions that may indicate possible misstatements, and
   - Critically assessing evidence.

10. Although the concept of professional skepticism is used to evaluate whether sufficient appropriate audit evidence has been obtained, and therefore whether audit risk has been reduced to an acceptably low level and consequently reasonable assurance has be obtained, the concept can be clearly distinguished from these and other related concepts in the ISAs. In particular, professional skepticism plays an important role in considering the persuasiveness of audit evidence.

[19] This is in line with the conclusion reached for IAASB Standards in Agenda Item 8-D "Supplemental Reference Material – for IAASB Information; Background Information Paper: Current Treatment of the Concept of Professional Skepticism in IAASB and IAESB Standards, the IESBA Code, and the IAASB ITC on Audit Quality", from the IAASB meeting in September 2016. https://www.iaasb.org/system/files/meetings/files/20160919-IAASB_Agenda_Item_8-D-Professsional_Skepticism_Supplemental_Reference.pdf

Appendix C

For Premise 2: Comparison and Analysis of Concept of Professional Skepticism to Fundamental Concepts in the Code

1. The IESBA Code of Ethics contains a number of concepts that may be related to the meaning of professional skepticism or that refer to professional skepticism. These comprise the fundamental principles of the Code and two concepts of independence as follows:[20]

Fundamental Principles of the Code

- **Integrity** – to be straightforward and honest in all professional and business relationships.
- **Objectivity** – to not allow bias, conflict of interest, or undue influence of others to override professional or business judgments.
- **Professional competence and due care** – to maintain professional knowledge and skill at a level required to ensure that a client or employer receives competent professional service based on current developments in practice, legislation and techniques and act diligently and in accordance with applicable technical and professional standards.
- **Confidentiality** – to respect the confidentiality of information acquired as a result of professional and business relationships and, therefore, not disclose any such information to third parties without proper and specific authority, unless there is a legal or professional right or duty to disclose, nor use the information for the personal advantage of the professional accountant or third parties.
- **Professional Behavior** – to comply with relevant laws and regulations and avoid any action that discredits the profession.

Independence

- **Independence of Mind** – The state of mind that permits the expression of a conclusion without being affected by influences that compromise professional judgment, thereby allowing an individual to act with integrity and exercise objectivity and professional skepticism.
- **Independence in Appearance** – The avoidance of facts and circumstances that are so significant that a reasonable and informed third party would be likely to conclude, weighing all the specific facts and circumstances, that a firm's, or a member of the audit team's integrity, objectivity or professional skepticism has been compromised.

2. The concept of professional skepticism is not defined in the current Code and, with one exception (relating to inadequate professional skepticism due to a self-review threat to independence resulting from a firm performing an audit or review of financial statements also providing internal audit

[20] IESBA Code of Ethics, paragraph 100.5 (for the fundamental principles) and paragraph 290.6 (for independence). Commensurate definitions of independence in relation to assurance engagements are provided, in paragraph 291.5 of the Code.

services),[21] is mentioned in the current Code only within the definitions of "independence of mind" and "independence in appearance". Both this exception and these definitions relate solely to audits and reviews or other assurance engagements – that is, the current Code does not extend professional skepticism to professional accountants that do not perform assurance engagements. The definition of **independence of mind** clarifies that it enables individuals to act with integrity and exercise objectivity and professional skepticism. This means that, based on the current definitions, the Code views independence of mind as a prerequisite for the integrity, objectivity and professional skepticism needed in an assurance engagement.

3. The fundamental principles of the Code, on the other hand, apply to all professional accountants, which implies that these principles also apply to practitioners performing assurance engagements. However, neither the ISAs nor the Code currently address the relationship between the fundamental principles and professional skepticism. The ISAs appear to treat compliance with the fundamental principles and independence as being in addition to, or in parallel to, the exercise of professional skepticism.[22]

4. In this context, it is important to recognize that many issues that are often subsumed under the concept of professional skepticism by academic and other literature are actually issues covered by the definitions of the fundamental principles of the Code.[23] For example, based on the definition of **integrity**, some deficiencies in auditor character and personal and cultural attributes may in part be issues related to integrity. Knowingly applying inadequate resources in an audit would also be in part a matter of integrity. Biases (including those resulting from framing, overconfidence, confirmation bias, anchoring, availability, dysfunctional group dynamics, incentives and disincentives) and conflicts of interest would be covered primarily by the definition of **objectivity**. Other deficiencies in auditor attributes may be related to inadequate **professional competence**. The fundamental principles of **confidentiality** and **professional behavior** appear to be less related to the concept of professional skepticism.

5. Even if an auditor has integrity, and is objective and professionally competent, an auditor nevertheless may not be sufficiently diligent in performing the audit. The principle of **due care** is described in the Code as the obligation to act diligently in accordance with applicable and professional standards when performing professional activities or providing professional services.[24] The Code describes diligence as encompassing the responsibility to act in accordance with the requirements of the assignment, carefully, thoroughly and on a timely basis.[25]

6. One of the major results arising from the analysis of responses to the ITC is the finding by the Joint PSWG that respondents identified impediments to the appropriate application of professional skepticism that were closely linked to the fundamental principles in the Code – in particular to

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21 IESBA Code of Ethics, paragraph 290.196

22 ISA 200 paragraph 14 in connection with ISA 200 paragraph A15, and ISA 200 paragraph 15.

23 See for example: "Enhancing Auditor Professional Skepticism" by Steven M. Glover and Douglas Prawitt, 2013, pp. 9-17; "Elevating Professional Judgment in Auditing and Accounting: The KPMG Professional Judgment Framework", KPMG, 2011, pp. 16-21; "A Model and Literature Review of Professional Skepticism in Auditing", Mark W. Nelson, 2009, pp. 7-9 and 11-15.

24 IESBA Code of Ethics, paragraph 130.1 (b)

25 IESBA Code of Ethics, paragraph 130.4

26 Agenda Item 8-A "Professional Skepticism – Issues (Including Feedback to the ITC) and Joint Working Group's Preliminary Recommendations on the Proposed Way Forward", paragraph 25.

objectivity – and to independence of mind. This suggests that the inappropriate application of professional skepticism might actually be indicative of inappropriate application of the fundamental principles of the Code or independence of mind. The fundamental principles and independence are covered in the ISAs, but not in any great detail. The question was posed whether enhancements to the ISAs or accounting firms' methodologies to more specifically address compliance with these fundamental principles and independence of mind could help improve the application of professional skepticism.[26]

7. In the context of the result that impediments to the appropriate application of professional skepticism appear to lie primarily in inadequate application of the fundamental principles and independence of mind, the question arises why – given the wide-ranging nature and power of the fundamental principles (in particular of integrity, objectivity, professional competence and due care) and of independence of mind – an additional concept of professional skepticism beyond the fundamental principles and independence of mind is needed for assurance engagements at all. What is it about assurance engagements that make them special so that they need an additional concept? What would that concept entail and does the current definition in the ISAs help in this respect?

8. Drawing on the analysis in **Appendix B**, the concept of professional skepticism extends beyond the concepts in the Code because it involves a questioning mind, being alert to conditions which may indicate possible misstatement, and a critical assessment of evidence – none of which are covered in the fundamental principles or independence as defined, but are important for the performance of assurance engagements. Consequently, even though the responses to the ITC suggest that the inappropriate application of professional skepticism might actually be indicative of inappropriate application of the fundamental principles of the Code or independence of mind, the concept of professional skepticism applicable to assurance engagements is separate from the concepts in the Code.

[26] Agenda Item 8-A "Professional Skepticism – Issues (Including Feedback to the ITC) and Joint Working Group's Preliminary Recommendations on the Proposed Way Forward", paragraph 25.

[27] Funk and Wagnall's Canadian College Dictionary, 1989, p. 1257

Appendix D

For Premise 3: Comparison and Analysis of Concept of Professional Skepticism to Professional Skepticism as Commonly Defined

1. Skepticism, other than philosophical skepticism, is defined in dictionaries along the following lines:

   - A doubting or incredulous state of mind; a disbelieving attitude[27]
   - Doubt as to the truth of some assertion or supposed fact[28]
   - An attitude of doubt or a disposition to incredulity either in general or toward a particular object[29]
   - Any questioning attitude or doubt towards one or more items of putative knowledge or belief.[30]

2. One dictionary provides the following treatment that is helpful in differentiating shades of meaning among some of the synonyms of "doubt" used above to describe the term "skepticism":

   "*Doubt, uncertainty, indecision, skepticism, incredulity, disbelief, suspicion, distrust* and *misgiving* refer to a state of mind that causes suspension of judgment or action. *Doubt* may be simple *uncertainty* about facts or truth, but usually combines also *indecision* about what action to take. *Skepticism* is a disposition to question, to demand evidence or proof before rendering judgment; it falls short of *incredulity*, which is unwillingness to believe what seems unlikely, and *disbelief*, which is the positive rejection of something alleged to be true or valid. We direct *suspicion* toward that which may be evil or wrong; *distrust* towards that which may be treacherous or deceitful. *Misgiving* is doubt about the outcome of an action." [31] [*Underlining not in original, but here for emphasis*]

3. To put these thoughts in another way, it appears that skepticism can be thought of as a disposition (a state or frame of mind) to question (i.e., to have or express uncertainty or doubt) and require evidence before drawing a conclusion. The common understanding of the concept of skepticism appears to turn on the need to obtain evidence to allay uncertainty or doubt.

4. In exploring an understanding of professional skepticism in a particular paper, one audit regulator (the FRC) explored the roots of the meaning of skepticism and drew on philosophical skepticism.[32] Without getting into the various philosophical theories of how to deal (or not to deal) with philosophical skepticism, most philosophical discussions about skepticism revolve around various versions of what philosophers call the "standard analysis" of knowledge involving questions about whether knowledge involves "justified true beliefs". The issue of justification is a central point of contention in these discussions: theories of justification often deal with what "adequate grounds" (i.e. "evidence") for

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[27] Funk and Wagnall's Canadian College Dictionary, 1989, p. 1257

[28] FRC, Auditing Practices Board, "Professional Scepticism: Establishing A Common Understanding and Reaffirming Its Central Role in Delivering Audit Quality", March 2012, p. 3, from the Shorter Oxford English Dictionary.

[29] Merriam-Websterhttps://www.merriam-webster.com/dictionary/skepticism, May 19, 2017

[30] https://en.wikipedia.org/wiki/Skepticism, May 19, 2017

[31] Funk and Wagnall's Canadian College Dictionary, 1989, p. 398

[32] FRC, Auditing Practices Board, "Professional Scepticism: Establishing A Common Understanding and Reaffirming Its Central Role in Delivering Audit Quality", March 2012, p. 3,

justification are.[33] Hence, addressing philosophical skepticism also involves questions about the need for evidence to address that skepticism.

5. In conclusion, both skepticism as commonly defined and understood as well as philosophical skepticism focus, at least in part, on the need to obtain evidence to address doubt. This begs the question as to what evidence is. Broadly speaking, evidence is understood as anything used to support or to undermine an assertion or claim. An assertion or claim is a form of information involving some kind of logical predication, such as "x is a cat".[34] What is it about the information that is being supported or undermined by evidence? Supporting or undermining information essentially means either increasing or decreasing, respectively, the **credibility** (that is, the degree to which something is worthy of belief) of that information. However, properly understood, evidence itself is a form of information (for even the use of "physical evidence" involves some predication about its attributes)[35]. This means that evidence is information that supports or undermines the credibility of other information. On this basis, it can be argued that skepticism as commonly understood involves the disposition question and need information (evidence) about the credibility of other information before drawing a conclusion on that credibility.

6. The current definition of **professional skepticism** also requires a disposition to question (a questioning mind) and in an assurance engagement, practitioners are required to obtain (sufficient appropriate) evidence prior to reaching a conclusion. However, based upon the definition of professional skepticism, what appears to set assurance engagements and professional skepticism apart from other activities of professional accountants, as well as from skepticism as commonly defined, appears to be:

   - Being alert to conditions which may indicate possible misstatement, and
   - A critical assessment of evidence.

7. The first bullet point goes beyond skepticism as commonly defined by, for example, requiring auditors to be alert for reasons why (i.e., the potential sources) the financial statements may be material misstatements (or as it is put colloquially in extant ISA 315 – "what can go wrong?"). This means that, for example, auditors do not just question, using common skepticism, whether the financial statements are prepared in accordance with the financial reporting framework – auditors must also be alert throughout the audit to the reasons why they might not be so prepared, which would affect the nature, timing and extent of the evidence (through risk assessment and response) that they would seek to obtain before drawing conclusions in relation to those financial statements.

8. The second bullet point appears to go beyond skepticism as commonly defined by clarifying, for example, that auditors are required to critically assess audit evidence. The requirement embodied in this definition begs the question as to what about audit evidence is supposed to be critically assessed. By using the application material in ISA 200 as a basis for further principles-based thinking about the issue, it could be argued that the salient feature of what makes audit evidence important in an audit – it persuasiveness – is what ought to be critically assessed by the auditor.[36] Hence, unlike for

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[33] See for example, Michael Williams, "Problems of Knowledge", Oxford University Press, 2001, pp. 15-25. [34] See FEE Issues Paper, "Principles of Assurance", 2003, pp. 79-80 in connection with pp. 204-208.

[34] See FEE Issues Paper, "Principles of Assurance", 2003, pp. 79-80 in connection with pp. 204-208.

[35] See FEE Issues Paper, "Principles of Assurance", 2003, p. 231-242.

[36] See ISA 200, paragraphs A22-A24.

skepticism as commonly defined, when exercising professional skepticism in an audit it is not enough to obtain evidence that supports or undermines the financial statements: auditors must also critically evaluate[37] whether the evidence obtained is sufficient and appropriate to reduce audit risk to an acceptably low level and thereby obtain reasonable assurance. This implies that auditors are required to perform procedures as necessary to be able to conclude whether the evidence obtained is persuasive enough (in terms of reliability, relevance and quantity) in the circumstances.

9. Hence, *what sets professional skepticism apart* from skepticism as commonly defined and understood (as well as from philosophical skepticism) is the 1. alertness to the sources of potential misstatements and 2. critical evaluation of whether evidence obtained is as persuasive as it needs to be. The former provides a basis for the application of a questioning mind about the credibility of the contents of the financial statements and helps drive the nature and extent of the evidence obtained (through risk assessment procedures and responses to assessed risks) needed to satisfy the auditor. The result of the latter (the critical evaluation) prompts an auditor to obtain additional evidence when the auditor concludes that the evidence is not as persuasive as it needs to be.

10. Consequently, the meaning of the term “professional skepticism” is NOT the combination of literal meaning of the adjective “professional” and of the noun “skepticism” as commonly defined and understood. Consequently, the term “professional skepticism” as currently defined does not mean “skepticism exercised by a professional (or professional accountant)”, but rather means exercising a questioning mind, being alert to conditions that may indicate possible misstatements, and critically assessing evidence, in an assurance engagement.

11. These points are central to what an assurance engagement is all about: alertness to, and consideration or assessment of risks of, material misstatement, and the need to seek to obtain evidence until the assurance practitioner concludes that the evidence obtained is persuasive enough. For these reasons, professional skepticism as currently defined in IAASB Standards is a crucial additional aspect of assurance engagements beyond skepticism as commonly defined.

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[37] Since the Clarity Project, the word “assess” has been restricted in the ISAs to assessment of risk, but the definition of “professional skepticism” was never changed to meet this policy. Hereafter, the term “evaluate” is used in line with this policy because the definition of “evaluate” in the Glossary of Terms aligns with the work effort in the ISAs on the sufficiency and appropriateness of evidence.

[37] Since the Clarity Project, the word “assess” has been restricted in the ISAs to assessment of risk, but the definition of “professional skepticism” was never changed to meet this policy. Hereafter, the term “evaluate” is used in line with this policy because the definition of “evaluate” in the Glossary of Terms aligns with the work effort in the ISAs on the sufficiency and appropriateness of evidence.

[38] Monitoring Group: IAIS, IOSCO; Member Bodies and Other Professional Organizations: AICPA, MAASB, FSR, ICAS

Appendix E

Respondents' Comments to the ITC on Whether There Should Be a More Fundamental Change to the Concept of Professional Skepticism

The following is an extract from the September 2016 IAASB meeting Agenda Item 8-A "Professional Skepticism – Issues (Including Feedback to the ITC) and Joint Working Group's Preliminary Recommendations on the Proposed Way Forward" of respondents' comments to the ITC suggesting that more fundamental changes to the concept of professional skepticism ought to be explored. These comments are relevant to the theme of "levels of professional skepticism".

1. Respondents who supported changing the definition suggested introducing a concept of a questioning mind that would tend to exhibit a more doubting or assertive attitude.[38] The words used in the ISAs could change the current confirmatory framework (obtain evidence to support management's assertions) to a framework which leads more to auditors seeking evidence both supporting and disconfirming management's assertions.[39]

2. One regulator also noted that the definition should be expanded to include:

   - Not only a questioning mind but one that robustly evaluates management's assertions;
   - Not only being alert to the potential for misstatement but also remaining open minded, probing and proactive about the potential for misstatement, notwithstanding past experience and the absence of manifest indicators of that potential having been realized;
   - Not only a critical appraisal of the evidence that management presents but also subjecting it to robust challenge through comparison with other relevant available sources of evidence whether those contradict or corroborate management's position.

3. Many respondents noted some change could be enacted through modifications to current ISAs. However, other respondents called for a more fundamental change to the concept of professional skepticism,[40] which may change the current model of an audit. The three most prevalent calls for action related to:

   - A change to a starting point to be a doubting mindset (sometimes referred to as "presumptive doubt");
   - A requirement to actively seek out contradictory evidence; and
   - Applying a continuum of professional skepticism that increases commensurate with the assessed risks of material misstatement.

[38] Monitoring Group: IAIS, IOSCO; Member Bodies and Other Professional Organizations: AICPA, MAASB, FSR, ICAS

[39] Monitoring Group: BCBS, IAIS

[40] Monitoring Group: BCBS, IAIS, IOSCO; Investors: IA; Regulators and Audit Oversight Authorities: ESMA, UKFRC; Member Bodies and Other Professional Organizations: AICPA; Academics: Glover-Prawitt

4. Some respondents believed the IAASB should explore whether the ISAs should more explicitly set out the concept of professional skepticism as a continuum,[41] rather than as an invariant concept. These respondents noted that the degree of professional skepticism throughout the audit might vary with risk identified and the professional judgments that were likely to be required (e.g., when auditing complex financial instruments or accounting estimates or other areas typically assessed as higher risks of material misstatement) – with linkage to the evidence that was expected to be obtained.

5. For example, as the risk of, and opportunity for, management reporting bias increases, there should be heightened professional skepticism and heightened skeptical actions taken by the auditor. The standards should incorporate the logic of a skepticism continuum that links higher levels of risk of material misstatement to more skeptical mindset and skeptical actions. The continuum would recognize that it is always important to have a questioning mind, but would clarify when the auditor should apply more or less of a challenging mindset and skeptical action.[42]

6. There were also respondents who noted the link between professional skepticism and risk assessment without explicitly referencing to a continuum.[43] A suggestion was made to link risk assessment and obtaining audit evidence more explicitly and in doing so give more prominence to paragraph A33 of ISA 240, which acknowledges ways in which increased professional skepticism can be exercised as part of the overall response to address the assessed risks of material misstatement due to fraud, as well as when more or less audit evidence may be obtained as a result of the auditor's assessment of risk. It was suggested to further clarify whether different "levels" of professional skepticism may be applied, and how this would relate to the current description of professional skepticism as an "attitude" or "mindset."[44]

[41] Regulators and Audit Oversight Authorities: ESMA; NSS: MAASB; Public Sector: GAO; Accounting Firms: PwC; Member Bodies and Other Professional Organizations: CAQ, FEE; Academics: AAA, Glover-Prawitt

[42] Member Bodies and Other Professional Organizations: AICPA, CAANZ, CAQ; Academics: Glover-Prawitt

[43] Member Bodies and Other Professional Organizations: ICAS

[44] Accounting Firms: KPMG

Agenda paper 6.2
AUASB Meeting 13 June 2017

Agenda Item 9-B

Strengthening the Pillars of Professional Skepticism

Observations of the IAASB-IAESB-IESBA Professional Skepticism Working Group

JUNE 2017

This publication has been prepared by the Professional Skepticism Working Group, which is comprised of representatives from the International Auditing and Assurance Standards Board (IAASB), International Ethics Standards Board for Accountants (IESBA), and the International Accounting Education Standards Board (IAESB).

It does not necessarily reflect the views of the boards themselves, does not constitute an authoritative pronouncement, nor does it amend, extend, or override the IAASB's International Standards,[1] the IESBA's Code of Ethics for Professional Accountants (the Code), or the IAESB's International Education Standards (IESs).

[1] The IAASB's International Standards is comprised of the International Standards on Quality Control, the International Standards on Auditing, the International Standards on Review Engagements, International Standards on Assurance Engagements, and the International Standards on Related Services.

Professional skepticism lies at the heart of a quality audit.

In 2015, the IAASB, IESBA, and IAESB convened a small, cross-representational working group—the Professional Skepticism Working Group—to formulate views on whether and how each of the three Boards' sets of international standards could further contribute to strengthening the understanding and application of the concept of professional skepticism as it applies to an audit.

Professional Skepticism is an attitude that includes a questioning mind, being alert to conditions which may indicate possible misstatement due to error or fraud, and a critical assessment of audit evidence.

ISA 200

Today, the topic of professional skepticism is featured prominently in each of the Board's strategic considerations, and all three Boards have important initiatives related to professional skepticism. All the Boards see the opportunity for shorter term actions as well as the need for longer term considerations, in consultation with each other.

The public interest in these initiatives is underscored by the increasing complexity of business and financial reporting, including the greater use of estimates and management judgments, changes in business models brought about by technological developments, and the fundamental reliance the public places on reliable financial reporting.

This publication presents several observations the Working Group believes are central to enhancing the exercise of professional skepticism in an audit. These observations are based on formal and informal feedback received by the Boards, input from academic research, and ideas from others offering insights—all aimed at enhancing the exercise of professional skepticism.

This publication also highlights actions of the three Boards regarding professional skepticism as it relates to auditors. For other professional accountants, the question has also been asked whether aspects of the concepts underlying professional skepticism also have relevance. Initiatives by the relevant Boards are therefore also noted.

OUR KEY OBSERVATIONS TO DATE

1. Business acumen is central to the exercise of professional skepticism.

In today's complex and rapidly changing business environment, strong business acumen is essential. For example, a deep knowledge of the client's business model, strong professional competencies, and a strong understanding of relevant standards; laws; and regulations enable robust professional skepticism. Education and continuing, impactful training remain vital.

2. Environmental factors can influence the ability to exercise professional skepticism.

Professional skepticism can be impeded by factors from tight financial reporting deadlines and resource constraints, to a firm's tone at the top and incentive systems, to local culture and groupthink. Heightening awareness of these and other factors is the first step to mitigate their impact.

3. Awareness of personal traits and biases is essential.

Personal traits play a role in the exercise of professional skepticism. These include, for example, confidence; an inquisitive nature; an individual's response to stress, time pressures, or conflict; knowledge; practical experience; and cultural background. Equally, a range of biases such as anchoring bias, confirmation bias and groupthink can act as impediments to the proper exercise of professional skepticism.

In consideration of these factors, standards might be improved by including more guidance about how an awareness and understanding of personal traits and biases can enhance the exercise of professional skepticism.

4. Building in professional skepticism from the outset is key.

Instilling professional skepticism starts at the beginning of one's career. For auditors, some have said it needs to be "part of their DNA."

Education and training can raise awareness and develop the needed attitude. At both the firm and engagement level, it is critical to reinforce and monitor the application of professional skepticism, including through setting the right tone at the top.

5. There is more that the three standard setting Boards can do, both in the immediate term and the longer term.

The Working Group has provided recommendations to all three Boards outlining actions that they may take individually as well as collectively. These included immediate actions, which are being acted on with priority attention, as well as considerations requiring further study.

A snapshot of the actions of the three standard-setting Boards is included in the section titled “Actions of the Standard Setters.”

6. Beyond audit, aspects of the concepts underlying professional skepticism may be relevant to all professional accountants

There have been questions about whether aspects of the concepts underlying professional skepticism should apply more broadly to all professional accountants, and not just auditors. There is a view that an understanding of the concepts underlying professional skepticism can benefit all professional accountants’ development. Also, it is observed that compliance with the fundamental principles in the Code can support the exercise of professional skepticism.

The Boards, in particular the IESBA and IAESB, recognize the need for further study about whether and, if so, how aspects of the concepts underlying professional skepticism should be pertinent to all professional accountants.

7. Standard setting alone is not enough.

All stakeholders with an interest in professional skepticism have a role to play to help cultivate a skeptical mindset.

We provide some specific thoughts about what others might do in the section titled “Standards Setting Alone Will Not Be Enough.”

STANDARD SETTERS' ACTIONS

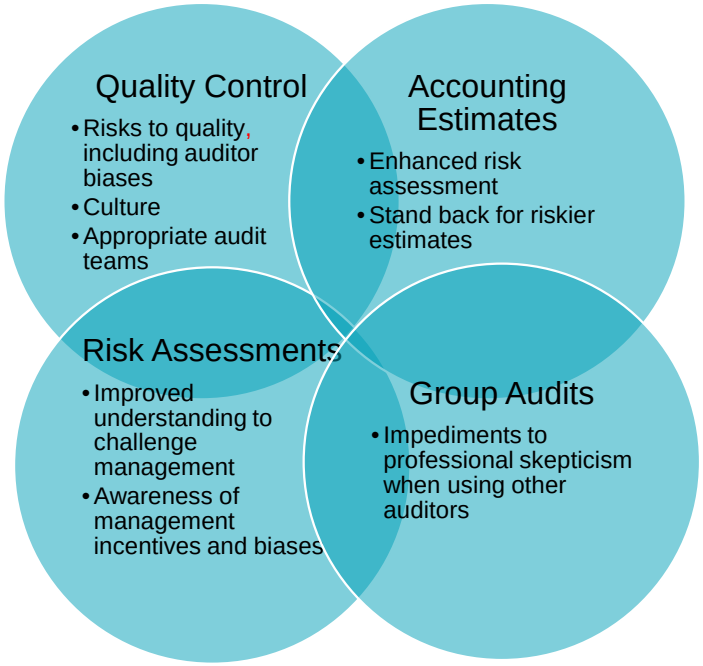
Each of the three standard setting Boards has acted on the inputs we and others provided regarding where further work or enhancements to the standards may provide benefit. The following is a snapshot of their immediate actions and longer term studies.

International Audit and Assurance Standards Board

The IAASB's International Standards already include many explicit references to professional skepticism. The IAASB's Professional Skepticism Q&A[2] highlights aspects of the ISAs that are particularly relevant to professional skepticism during an audit of financial statements. It also highlights the role of others in supporting professional skepticism.

The IAASB focuses on professional skepticism in every project. This is more than just referring to it—it involves looking for opportunities to embody the expectation of professional skepticism into the design of the requirements, and to challenge whether the standard can do more to promote professional skepticism.

Professional skepticism focus areas in current IAASB projects include:



[2] *Staff Questions & Answers – Professional Skepticism in an Audit of Financial Statements*, February 2012

International Ethics Standards Board for Accountants

The IESBA is committed to clarifying the behavior that is expected of all professional accountants in the public interest.

With respect to auditors and assurance practitioners, as an initial step, the IESBA's April 2017 Exposure Draft (ED), *Proposed Application Material Related to Professional Skepticism and Professional Judgment* proposes guidance that clarifies how compliance with the fundamental embodied in the Code supports the exercise of professional skepticism in the context of audits, reviews and other assurance engagements.

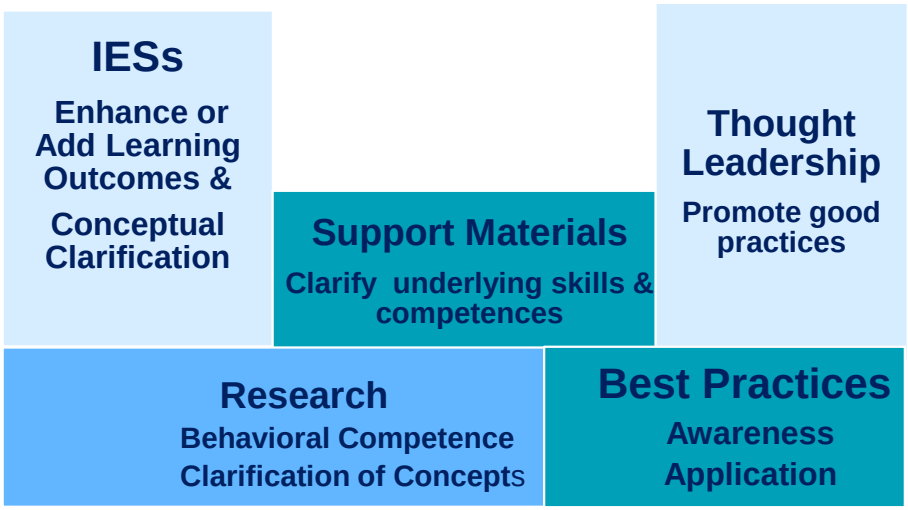
More broadly, the ED also proposes guidance that emphasizes the importance of professional accountants obtaining a sufficient understanding of the facts and circumstances known to them when exercising professional judgment in the context of complying with the fundamental principles.

While the IESBA's efforts in the short term will be informed by the feedback on the May 2017 ED, the IESBA intends to consider as part of a longer term initiative whether there is a public interest need to develop material to describe the role and expectations of professional accountants. [This will include how their work contributes to enhancing the integrity and reliability of information with which they are associated. ****Subject to further refinement after the June IESBA meeting***]

International Accounting Education Standards Board

The IAESB is committed to developing its IESs and supporting materials to enhance the skills and competence needed to apply professional skepticism.

As shown in the accompanying graphic, the IAESB will undertake research and gather examples of best practices. The IAESB will also engage with stakeholders to decide how best to promulgate and support the education and training needed to improve the application of professional skepticism. Outputs from this process may include a review of



research, revisions to the IESs, support materials, thought leadership, and development of best practice materials.

These initiatives will help inform the IAESB's consideration of how these efforts can inform the future development of IESs to better build behavioral competence. Looking ahead, the IAESB will consider what needs to be done to enable individuals to meet the requirements and expectations set out in other standards and the expectations of the public.

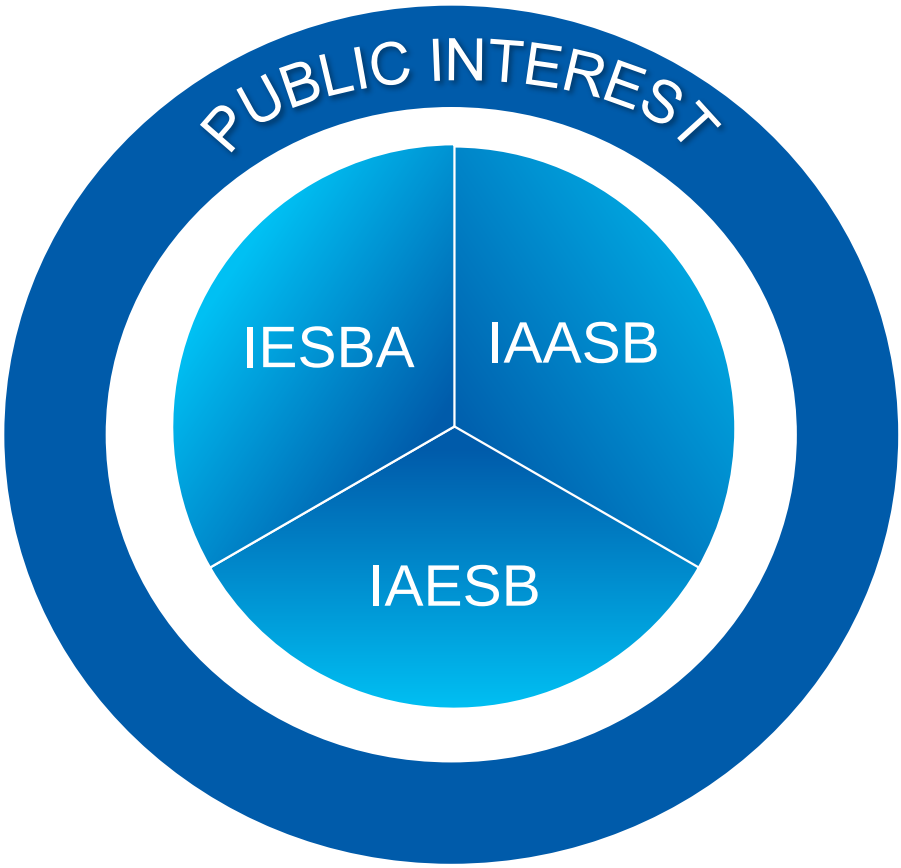
THE JOURNEY FORWARD

The work of the Boards on professional skepticism has been a journey, and there is still further to travel. The Working Group believes that in serving the public interest and in satisfying their mutual obligation to address the issues highlighted in this paper, the Boards' efforts should be undertaken in close consultation with each other.

If behavioral change is needed, it is necessary to carefully study how to effect it.

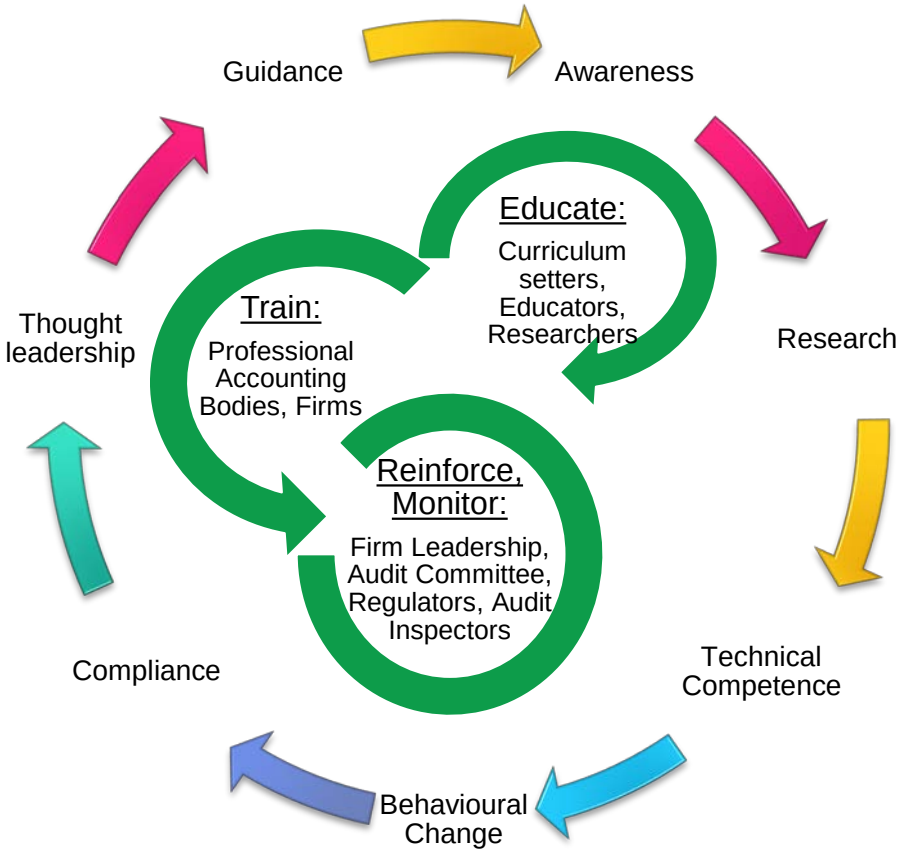
For the IAASB, whose remit includes audit, assurance, and related services, this means considering and analyzing the merits of fundamental changes to the concept and definition of professional skepticism in light of the public's expectations. This is particularly around how the definition relates to the critical assessment of audit evidence, and documentation.

For the IESBA and the IAESB, their remits include all professional accountants, not just auditors. These Boards have been challenged as to whether the IAASB's concept of professional skepticism, or aspects thereof – such as the "questioning mindset" – has relevance to professional accountants who do not perform audits or other assurance engagements.



STANDARD SETTING ALONE WILL NOT BE ENOUGH

All stakeholders that have an interest in high quality financial reporting and auditing, and an interest in professional skepticism, have a role to play to help cultivate a skeptical mindset. For some, including firms, this means educating or training more junior staff on what "good" professional skepticism looks like in practice. For others, such as audit committees, it may mean continuing to challenge auditors to ask tough questions of management.



The three standard setting boards will continue to liaise with stakeholders to improve their understanding of, and support for, professional skepticism.

The Working Group is grateful to all those that have engaged with us and the three standard setting Boards to date. This includes the special guest speakers from academia and inspectors that have presented to the three standards setting Boards, all commentators on the discussion papers from the Boards, and others that have engaged with the Working Group through the journey. Continued support from all stakeholders will be necessary to advance professional skepticism.

PROFESSIONAL SKEPTICISM WORKING GROUP

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IAASB International Auditing and Assurance Standards Board

www.iaasb.org

Meeting: IAASB

Meeting Location: New York, USA

Meeting Date: June 19–22, 2017

Agenda Item 8

Data Analytics—Issues and Discussion

Objective of Agenda Item

1. The objective of this Agenda Item is to provide the IAASB with high level observations from the comment letters received from the *Request for Input: Exploring the Growing Use of Technology in the Audit, with a Focus on Data Analytics*.

2. The Data Analytics Working Group (DAWG) comprises the following members:

   - Bob Dohrer, IAASB Member and Chair of the DAWG;
   - Fiona Campbell, IAASB Member;
   - Sue Almond, Partner, Grant Thornton;
   - Peter Eimers, Partner, PricewaterhouseCoopers; and
   - Alan Young, Partner, Ernst and Young.

Activities since the Last IAASB Discussion

3. The Chair of the DAWG and Staff participated in a teleconference with the Public Company Accounting Oversight Board on Data Analytics.

4. The Chair of the DAWG participated in a panel discussion titled “Trusted Financial System of the Future” that featured a discussion about data analytics during the Contabilidad y Responsabilidad para el Crecimiento Económico Regional Conference 2017 in Mexico City.

5. The comment period for the request for input closed on February 15, 2017, and 50 responses were received. The responses received can be accessed through the IAASB Data Analytics project page. The Appendix to this Agenda Item includes the list of respondents.

Matters for IAASB Consideration

6. A presentation will be provided in advance of the IAASB meeting.

Appendix

List of respondents to the Request for Input

Members of the monitoring group are marked with an asterisk (*).

Investors and Analysts

1. CFA Institute
2. EXPERT Suisse
3. Harvest Investments

Regulators and Oversight Authorities

4. International Association of Insurance Supervisors*
5. International Forum of Independent Audit Regulators*
6. Independent Regulatory Board for Auditors (South Africa)
7. United Kingdom Financial Reporting Council

National Auditing Standard Setters

8. Australian Auditing and Assurance Standards Board
9. Canadian Auditing and Assurance Standards Board
10. Compagnie Nationale des Commissaires aux Comptes and the Conseil Superieur de l'Ordre des Experts-Comptables
11. Institut der Wirtschaftspruefer
12. The National Association of State Boards of Accountancy's
13. The Japanese Institute of Certified Public Accountants
14. Auditing and Assurance Standards Board of Malaysian Institute of Accountants
15. Nederlandse Beroepsorganisatie van Accountants
16. New Zealand Auditing and Assurance Standards Board

Accounting Firms

17. BDO International Limited
18. Baker Tilly UK Audit LLP
19. Crowe Horwath International
20. Deloitte Touche Tohmatsu Limited
21. Ernst & Young Global Limited
22. Grant Thornton International Limited
23. KPMG IFRG Limited (Network)

24. Moore Stephens LLP (United Kingdom firm)
25. PKF International Limited
26. PricewaterhouseCoopers International Limited

Public Sector Organizations

27. Auditor General of Alberta
28. Auditor General of New Zealand
29. Chartered Institute of Public Finance and Accountancy

Member Bodies and Other Professional Organizations

30. Accountancy Europe
31. Association of Chartered Certified Accountants
32. American Institute of Certified Public Accountants
33. Chartered Accountants Australia and New Zealand
34. Chartered Professional Accountants of Canada
35. CPA Australia
36. European Federation of Accountants and Auditors for SMEs
37. Institute of Chartered Accountants in England and Wales
38. Institute of Chartered Accountants of Scotland
39. The Institute of Singapore Chartered
40. Malta Institute of Accountants
41. Pennsylvania Institute of Certified Public Accountants
42. South African Institute of Chartered Accountants
43. IFAC Small and Medium Practices Committee

Academics

44. Hunter College Advanced Auditing Class at the Graduate School (Joseph A. Maffia)
45. Rutgers, The State University of New Jersey (Accounting and Information Systems Department)

Individuals and Others

46. Denise Silva Ferreira Juvenal
47. Inflo Software
48. Shigeto Fukuda, CISA
49. Tom Koning

50. The Technology Solutions and Practices (TSP) Committee of the Institute of Management Accountants (IMA)