



AUASB Board Meeting Summary Paper

AGENDA ITEM NO. 2.0
Meeting Date: 10 March 2020
Subject: Proposed ISA 600 Group Audits
Date Prepared: 2 March 2020
Prepared by: Rene Herman

Action Required

For Information Purposes Only

A. Background

- 1 In December 2016 and following on from the IAASB's Invitation to Comment, the IAASB approved a project proposal to revise ISA 600.
- 2 The key points raised by the AUASB in the invitation to comment included the following:
 - (a) At the time of the ITC, the AUASB supported a combination of a top down/bottom up approach to scoping of group audits. Since the progression of ISA 315, the AUASB supports a top down risk-based approach – with audit effort responsive to the risk of material misstatement. Refer 3(a) below.
 - (b) Explanation on elements of ISA 600 applicability where the component auditor is the group auditor – refer comments on new structure of the standard, refer C.1 below.
 - (c) Broadening to ISA to include all types of structures including for example branches, divisions, joint ventures – refer comments on definitions and applicability of the standard, refer C.2 below.
 - (d) Guidance on practical access issues, refer C.3 below.
 - (e) The involvement of the group engagement partner (GEP) to direct and supervise the component teams work; and additional application material on communications upward from the component auditor to the group auditor could be strengthened as the group auditor is not necessarily the best placed to determine and understand the significant risks at a component level. Refer C.4 below.
 - (f) Guidance required in relation to component materiality, component performance materiality and component trivial thresholds, particularly in relation to the concept of aggregation risk, refer C.5 below.
 - (g) Guidance as to extent of documentation of the GETs involvement in the work of component auditors, refer C.6 below.

This document contains preliminary views and/or AUASB Technical Group recommendations to be considered at a meeting of the AUASB and does not necessarily reflect the final decisions of the AUASB. No responsibility is taken for the results of actions or omissions to act on the basis of reliance on any information contained in this document (including any attachments), or for any errors or omissions in it.

- 3 At the June IAASB meeting, the IAASB agreed the following principles to the revision to ISA 600:
- (a) a risk-based approach to ISA 600 aligned to ISA 315– to this end, the current drafting of ISA 600 has removed the definition and concepts behind significant components.
 - (b) making the drafting specific to special considerations for a group audit and not repeating the requirements of the foundational standards, that is draft requirements to address the special considerations (incremental to requirements of other ISAs).

B. What the Audit Technical Group (ATG) is seeking from the AUASB at the March 2020 AUASB meeting

4 The IAASB is expected to vote on ED-ISA 600 at the March 2020 IAASB meeting, accordingly, the March 2020 IAASB meeting is an important meeting for any significant comments in relation to the finalisation of the draft proposed standard. In line with the AUASB international influencing strategy, AUASB members are encouraged to comment on any areas of the proposed standard covered in the body of this summary paper; as well as on the full draft proposed ISA 600 to inform the AUASB Chair of their views.

5 The purpose of this Agenda Item is to update the AUASB as to progress made by the ISA 600 taskforce particularly in the areas of:

- (a) Structure of the standard, C.1 below.
- (b) Definitional changes, C.2 below.
- (c) Access, C.3 below.
- (d) Involvement of the GEP, C.4 below.
- (e) Materiality, C.4 below.
- (f) Documentation; C.5 below.

6 Additionally, the AUASB is asked to consider the Exposure process in Australia as outlined in E.28 below.

7 A link to a clean copy of ISA 600 can be found [[here](#)]; a clean copy of ISA 600 is also included at Agenda Item 2.1.

C. Where the Proposed ISA 600 is at in relation to the matters outlined at paragraph 5

C.1 Structure of the revised standard

8 The standard has been structured so that each section of the standard has a sub-section that describes the considerations when component auditors are involved as applicable. This is a change from the previous drafts of this document where there was a complete separate section relating to the involvement of component auditors. The reason for the change is to make it clearer which interactions are needed between the group and component auditor throughout the stages of the engagement; and demonstrates that component auditors are integral and need to be involved throughout the audit.

9 The ATG raises no concerns in relation to the structure of the revised standard having seen the development of the standard both ways, supports this latest development.

C.2 Definitions

- 10 The standard applies to the audit of group financial statements and special considerations when component auditors are involved. The following revised definitions are relevant to the scope and audit of the standard:
- (i) Group financial statements – Financial statements that include the financial information of more than one entity or business unit through a consolidation process.
 - (ii) Component – a location, function or activity (or combination of locations, functions or activities) determined by the group engagement team for purposes of planning and performing audit procedures in a group audit.
 - (iii) Consolidation process – for purposes of ISA 600 this includes consolidation, proportionate consolidation, equity methods accounting, the aggregation of financial information of branches, division, other entities or business units.
- 11 The entry point into the standard, i.e. where ISA 600 applies is when the auditor has been engaged to audit group financial statements i.e.: the preparation of group financial statements is the entry point into the standard – management perspective.
- 12 Once ISA 600 applies, the auditor then determines an appropriate approach to planning and performing the audit – for this purpose the group engagement team uses judgement in determining the components for which audit procedures will be performed (which may or may not align with the way a group is organised for management purposes); i.e. components are determined from the auditors perspective.
- 13 The Audit Technical Group raises no concerns with these definitions or the implications of the use of the definitions through the standard. The ATG supports that these definitions greatly assist with the scoping of standard. The AUASB is referred to paragraphs 2, A4 and A6 of the proposed ISA 600. The ATG considers that the requirements and application material address the AUASB matters raised at the time of the Invitation to Comment.

14	Question 1 for the AUASB: Does the AUASB agree with the definitions of group financial statements and component in ISA 600?
----	--

C.3 Access

- 15 The special considerations for the terms of engagement for a group audit, relates to group management acknowledging and understanding its responsibility to provide the engagement team with unrestricted access to people or information.
- 16 There is new application material that:
- highlights that access to people and/or information can be restricted;
 - focuses on how the GET may overcome such issues;
 - indicates that the GET may communicate restrictions with regulators, listing authorities or other – particularly where restrictions affect multiple auditors in a jurisdiction or by the same firm;
 - focuses on the effects when the GET cannot overcome restrictions and ultimately explains that access restrictions do not alleviate the requirement for the GET to obtain sufficient appropriate audit evidence; and

- highlights where there are access restrictions related to an equity-accounted investment and guidance on how the GET may overcome such restrictions
- 17 The AUASB is referred to requirements of paragraphs 14-17 and associated guidance particularly paragraphs A24 – A31 of Proposed ISA 600. The ATG raises concerns with reference to the application guidance of paragraph A27 where the GET may communicate restrictions with regulators, listing authorities or other – particularly where restrictions affect multiple auditors in a jurisdiction or by the same firm. Besides A27, the ATG considers that the requirements and application material address the AUASB matters raised at the time of the Invitation to Comment.

<p>18 Question 2 for the AUASB: Does the AUASB support the way that access has been addressed in Proposed ISA 600 and the new application material included at paragraph A27?</p>
--

C.4 *The involvement of the group engagement team (GET) to direct and supervise the component teams work and more guidance in relation to communication upwards from the Component Auditor*

19 Tighter linkage to Proposed ISA 220 including:

- (a) Requirement for GEP sufficiently and appropriately involved throughout the group audit engagement with application material recognising that ISA 220 allows for the assignment of responsibilities.
- (b) Requirement for GEP to determining that component auditors have appropriate competency and capability – extensive application material provided.
- (c) Requirement for the GET to take responsibility for the nature, timing and extent of direction and supervision of component auditors – while recognising the scalability of this in relation to risk and judgement – extensive application material provided.

20 Refined requirements and additional application material regarding upwards communication from the Component Auditor to the GET. Downward communications from the GET to the component auditor is dealt with in each of the sub-sections that describes the special considerations when component auditors are involved.

C.5 *Materiality*

21 Feedback from the ITC indicated that there is confusion and variation in practice relating to the auditor’s understanding of the concepts of component materiality, component performance materiality and clearly trivial thresholds and that aggregation risk is not well understood. To address this, the following changes have been proposed to ISA 600:

- (a) Aggregation Risk:
 - New definition included at paragraph 7(a) of ISA 600
 - Paragraph A9 has been included to demonstrate that in a group engagement there is a greater likelihood that audit procedures will be performed on accounts, classes of transactions or disclosures that are disaggregated across components – essentially aggregation risk increases as the number of components increases.
- (b) Component materiality

- Component materiality has been replaced with component performance materiality including a definition change. Materiality used in performing audit procedures on disaggregated component financial information is better described as component performance materiality and is expected to cause less confusion.
 - The requirement of paragraph 26(a)) is clear that component performance materiality is less than group performance materiality. There is application material in paragraph A72 that describes the factors that the GET may consider in setting component performance materiality – focussing on aggregation risk and expectations about nature, frequency and magnitude of misstatements.
- (c) Clearly trivial threshold
- To address regulator concerns the requirement of paragraph 26(b) indicates that clearly trivial thresholds at the component level shall not exceed the threshold at the group level.

C.5 Documentation

- 22 The requirements and application material in relation to documentation have been expanded, refer paragraph 53 and A124- A130. The Taskforce has added application material to address circumstances in which the GET is restricted from including CA documentation in its audit file and therefore certain important aspects of the component auditor documentation would not be available to an experienced auditor. In this scenarios, the GET uses professional judgement in determining the nature and extent of documentation on file The ATGs view is that application material could still be extended to address the regulators concerns regarding the extent of inclusion of component auditor’s work papers retained on audit files. The taskforce considers the questions on exposure will need to address whether more guidance is considered necessary and if so, suggestions for such additional guidance.

23 **Question 3 for the AUASB: Does the AUASB consider that more guidance is warranted in relation to Proposed ISA 600? If so, what suggestions does the AUASB have?**

D. Other aspects of the standard

- 24 Understanding the entity and its environment, the applicable reporting framework and the entity’s system of internal control; Identifying and Assessing the Risks of Material Misstatement; and Responding to the Assessed risks of Material Misstatement
- (a) Close alignment to ISA 315.
 - (b) Extensive guidance regarding common controls (extant was group wide controls) – A52-A54.
 - (c) Extensive guidance on centralised activities (including shared service centres) – A55-A65.

25 **Question 4 for the AUASB: Does the AUASB support the guidance included on common controls and centralised activities?**

E. Way forward

- 26 If Proposed ISA 600 is voted for issuance at the March 2020 IAASB meeting, the taskforce considers that the ED will be published around 23 April 2020 with a closing date of 11 August 2020. The taskforce is recommending a 110-day exposure period so that the taskforce can bring high level feedback to the September 2020 IAASB meeting and aim to approve to issue the final standard at the June 2021 IAASB meeting.

- 27 The taskforce is suggesting that the effective date for ISA 600 aligns with the effective date of the QM standards, that is for period beginning on or after 15 December 2022. The taskforce is proposing asking a question on ED regarding the effective date.
- 28 Consistent with the process adopted for ISA 315 and the Quality Management suite of standards, and in order to obtain timely stakeholder feedback to influence the IAASB standard-setting process, the ATG is recommending that ED-ASA 600 is exposed at the same time as ED-ISA 600. As the final ED-ISA 600 may only become available to the ATG after the 21 April 2020 AUASB meeting, a more detailed timeframe and outreach plan will be presented to the AUASB in due course.

Proposed ISA 600 (Revised), *Special Considerations—Audits of Group Financial Statements (Including the Work of Component Auditors)* – Clean

Introduction

Scope of this ISA

1. This ISA deals with special considerations that apply to an audit of group financial statements, including in those circumstances when component auditors are involved. The requirements and guidance in this ISA refer to, or expand on, how other relevant ISAs are to be applied in relation to an audit of group financial statements (group audits), in particular proposed ISA 220 (Revised),¹ ISA 315 (Revised 2019),² and ISA 330.³ (Ref: Para. A1–A2)
2. Groups may be organized in various ways. For example, groups may organize their activities geographically, by business units, economic units, or business activities, which are referred to as “entities or business units” in this ISA. This ISA applies when, based on the entity’s structure and the requirements of the applicable financial reporting framework, the group financial statements include the financial information of more than one entity or business unit through a consolidation process. The auditor may plan and perform an audit of group financial statements based on the entities or business units as viewed by group management. Alternatively, the group engagement team may determine that it is more effective or efficient to plan and perform the group audit based on locations, functions or activities that are not necessarily aligned with how group management views the entities or business units comprising the group. This ISA uses the term “component” to refer to the manner in which the group engagement team views the group structure for purposes of planning and performing audit procedures for the group audit. (Ref: Para. A4–A6)
3. This ISA recognizes that component auditors can be, and often are, involved in the group audit to assist the group engagement team in identifying, assessing and responding to the risks of material misstatement of the group financial statements. Accordingly, this ISA requires sufficient and appropriate involvement by the group engagement team in the work of component auditors and emphasizes the importance of two-way communication between the group engagement team and component auditors. In addition, this ISA explains the matters that the group engagement team takes into account when determining the nature, timing and extent of the direction and supervision of component auditors and the review of their work. (Ref: Para. A7–A8)
4. When this ISA expressly intends that a requirement or responsibility be fulfilled by the group engagement partner or the group engagement team, the term “the group engagement partner shall ...” or “the group engagement team shall ...” is used. When the group engagement partner or the group engagement team is permitted to assign the design or performance of procedures, tasks or actions to appropriately skilled or suitably experienced members of the engagement team, including component auditors, the term “the group engagement partner shall take responsibility for...” or “the group engagement team shall take responsibility for...”

¹ Proposed ISA 220 (Revised), *Quality Management for an Audit of Financial Statements*. All References to proposed ISA 220 (Revised) are to the version presented to the IAASB in March 2020.

² ISA 315 (Revised 2019), *Identifying and Assessing the Risks of Material Misstatement*

³ ISA 330, *The Auditor’s Responses to Assessed Risks*

is used. Nevertheless, the group engagement partner remains ultimately responsible, and therefore accountable, for compliance with the requirements of this ISA.

Effective Date

5. This ISA is effective for audits of group financial statements for periods beginning on or after December 15, 20XX.

Objectives

6. The objectives of the auditor are:
 - (a) With respect to the acceptance and continuance of the group audit engagement, to determine whether sufficient appropriate audit evidence can reasonably be expected to be obtained to provide a basis for the opinion on the group financial statements;
 - (b) To identify and assess the risks of material misstatement of the group financial statements, and to plan and perform further audit procedures to appropriately respond to those assessed risks;
 - (c) To evaluate whether sufficient appropriate audit evidence has been obtained from the audit procedures performed, including with respect to the work performed by component auditors, as a basis for an opinion on the group financial statements; and
 - (d) To be sufficiently and appropriately involved in the work of component auditors throughout the group audit engagement, including communicating clearly about the scope and timing of their work, and in evaluating the results of that work.

Definitions

7. For purposes of the ISAs, the following terms have the meanings attributed below:
 - (a) Aggregation risk – The probability that the aggregate of uncorrected and undetected misstatements exceeds materiality for the financial statements as a whole. (Ref: Para. A9)
 - (b) Component – A location, function or activity (or combination of locations, functions or activities) determined by the group engagement team for purposes of planning and performing audit procedures in a group audit.
 - (c) Component auditor – An auditor who, at the request of the group engagement team, performs audit procedures related to a component for purposes of the group audit. A component auditor is a subset of the engagement team.⁴ (Ref: Para. A10–A11)
 - (d) Component management – Management responsible for a component.
 - (e) Component performance materiality – An amount or amounts set by the group engagement team to reduce aggregation risk to an appropriately low level for purposes of planning and performing audit procedures in relation to a component.
 - (f) Group – An entity for which group financial statements are prepared.
 - (g) Group audit – The audit of group financial statements.
 - (h) Group audit opinion – The audit opinion on the group financial statements.

⁴ Proposed ISA 220 (Revised), paragraph 10(d)

- (i) Group engagement partner – The engagement partner⁵ who is responsible for the group audit.
 - (j) Group engagement team – A subset of the engagement team that includes partners (including the group engagement partner) and staff who:
 - (i) Establish the overall group audit strategy and audit plan;
 - (ii) Direct and supervise component auditors and review their work; and
 - (iii) Evaluate the conclusions drawn from the audit evidence obtained as the basis for forming an opinion on the group financial statements.
 - (k) Group financial statements – Financial statements that include the financial information of more than one entity or business unit through a consolidation process.
 - (l) Group management – Management responsible for the preparation of the group financial statements.
 - (m) Group performance materiality – Performance materiality⁶ in relation to the group financial statements as a whole, as determined by the group engagement team.
8. Reference in this ISA to “the applicable financial reporting framework” means the financial reporting framework that applies to the group financial statements.
9. Reference in this ISA to “the consolidation process” includes the recognition, measurement, presentation, and disclosure, in accordance with the requirements of the applicable financial reporting framework, of financial information of entities or business units in the group financial statements by way of: (Ref: Para. A12, A14)
- (a) Consolidation, proportionate consolidation, or the equity methods of accounting;
 - (b) The aggregation of the financial information of branches or divisions; or (Ref: Para. A13)
 - (c) The presentation in combined financial statements of the financial information of entities or business units that have no parent but are under common control.

Requirements

Leadership Responsibilities for Managing and Achieving Quality on a Group Audit

10. In applying proposed ISA 220 (Revised),⁷ the group engagement partner shall be sufficiently and appropriately involved throughout the group audit engagement, including in the work of component auditors, such that the group engagement partner has the basis for determining whether the significant judgments made and the conclusions reached are appropriate given the nature and circumstances of the group audit engagement. (Ref: Para. A15–A16)

⁵ Proposed ISA 220 (Revised), paragraph 10(a)

⁶ ISA 320, *Materiality in Planning and Performing an Audit*, paragraph 11

⁷ Proposed ISA 220 (Revised), paragraph 13

Acceptance and Continuance

11. The group engagement partner shall determine whether sufficient appropriate audit evidence can reasonably be expected to be obtained to provide a basis for the opinion on the group financial statements. (Ref: Para. A17–A20)
12. If, after the acceptance or continuance of the group audit engagement, the group engagement partner concludes that sufficient appropriate audit evidence cannot be obtained, the group engagement partner shall consider the possible effects on the group audit. (Ref: Para. A21)

Terms of the Engagement

13. In applying ISA 210,⁸ the group engagement team shall obtain the agreement of group management that it acknowledges and understands its responsibility to provide the engagement team with: (Ref: Para. A22–A23)
 - (a) Access to all information of which group management is aware that is relevant to the preparation of the group financial statements such as records, documentation and other matters;
 - (b) Additional information that the engagement team may request from management for the purpose of the group audit; and
 - (c) Unrestricted access to persons within the group from whom the engagement team determines it necessary to obtain audit evidence.

Restrictions on Access Outside the Control of Group Management

14. If the group engagement partner concludes that group management cannot provide the engagement team with unrestricted access to information or persons within the group due to restrictions that are outside the control of group management, the group engagement partner shall consider the possible effects on the group audit. (Ref: Para. A24–A28)

Restrictions on Access Imposed by Group Management

15. If the group engagement partner concludes that:
 - (a) It will not be possible for the group engagement team to obtain sufficient appropriate audit evidence due to restrictions imposed by group management; and
 - (b) The possible effect of this limitation will result in a disclaimer of opinion on the group financial statements,the group engagement partner shall either:
 - (a) In the case of a new engagement, not accept the engagement, or, in the case of a continuing engagement, withdraw from the engagement, where withdrawal is possible under applicable laws or regulations; or
 - (b) Where laws or regulations prohibit an auditor from declining an engagement or where withdrawal from an engagement is not otherwise possible, having performed the audit of the group financial statements to the extent possible, disclaim an opinion on the group financial statements. (Ref: Para. A29–A30)

⁸ ISA 210, *Agreeing the Terms of Audit Engagements*, paragraph 6(b)

Considerations When Component Auditors Are Involved

16. In applying proposed ISA 220 (Revised),⁹ the group engagement partner shall evaluate whether the group engagement team will be able to be involved in the work of the component auditor to the extent necessary to obtain sufficient appropriate audit evidence. (Ref: Para. A31)
17. The group engagement team shall request the component auditor to confirm that the component auditor will cooperate with the group engagement team.

Relevant Ethical Requirements

18. In applying proposed ISA 220 (Revised),¹⁰ the group engagement partner shall take responsibility for: (Ref: Para. A32–A34, A112)
 - (a) Determining that the component auditor has been made aware of relevant ethical requirements that are applicable given the nature and circumstances of the group audit engagement;
 - (b) Obtaining an understanding about whether the component auditors understand and will comply with the ethical requirements that are relevant to the group audit engagement and, in particular, are independent; and
 - (c) Prior to dating the auditor's report, obtaining a confirmation from component auditors that the ethical requirements that are relevant to the group audit engagement, including those related to independence, have been fulfilled.

Engagement Resources

19. In applying proposed ISA 220 (Revised),¹¹ the group engagement partner shall: (Ref: Para. A35)
 - (a) Determine that component auditors have the appropriate competence and capabilities, including sufficient time to perform the assigned procedures at the component; and (Ref: Para. A36–A41)
 - (b) When information can be obtained about the results of the monitoring and remediation process or external inspections with respect to the component auditor's firm, determine the relevance of such information to, and effect on, the group audit. (Ref: Para. A42–A43)
20. If a component auditor does not meet the independence requirements that are relevant to the group audit, or the group engagement partner has serious concerns about any of the matters in paragraphs 16, 18 and 19, the group engagement team shall obtain sufficient appropriate audit evidence relating to the work to be performed at the component without involving that component auditor. (Ref: Para. A44–A45)

Engagement Performance

21. In applying proposed ISA 220 (Revised),¹² the group engagement partner shall take responsibility for the nature, timing and extent of direction and supervision of component

⁹ Proposed ISA 220 (Revised), paragraph 13

¹⁰ Proposed ISA 220 (Revised), paragraph 16-17, 21

¹¹ Proposed ISA 220 (Revised), paragraph 25-26

¹² Proposed ISA 220 (Revised), paragraph 29

auditors and the review of their work. In doing so, the group engagement partner takes into account areas: (Ref: Para. A46–A48)

- (a) Where the assessed risk of material misstatement of the group financial statements is higher on the spectrum of risk or where a significant risk has been identified; and
- (b) In the group financial statements that involve significant judgment.

Understanding the Group and Its Environment, the Applicable Financial Reporting Framework and the Group’s System of Internal Control

22. In applying ISA 315 (Revised 2019),¹³ the group engagement team shall take responsibility for obtaining an understanding of the following: (Ref: Para. A49–A51, A66–A67)

- (a) The group and its environment, including: (Ref: Para. A52–A54)
 - (i) The group’s organizational structure and its business model, including:
 - a. The locations in which the group has its operations or activities;
 - b. The nature and similarities of the group’s activities and business lines; and
 - c. The extent to which the group’s business model integrates the use of IT; and
 - (ii) The nature and extent of the measures used internally and externally to assess the entities or business units’ financial performance;
- (b) The applicable financial reporting framework, including the consistency of accounting policies and practices across the group; and
- (c) The group’s system of internal control, including:
 - (i) The nature and extent of commonality of controls; (Ref: Para. A55–A60)
 - (ii) Whether, and if so, how, the group centralizes activities; (Ref: Para. A61–A62)
 - (iii) The consolidation process used by the group, including sub-consolidations, if any, and consolidation adjustments; and
 - (iv) How the group management communicates significant matters that support the preparation of the group financial statements and related reporting responsibilities in the information system and other components of the group’s system of internal control. (Ref: Para. A63–A65)

Considerations When Component Auditors Are Involved

23. When risk assessment procedures are assigned to component auditors, the group engagement team shall discuss with component auditors matters related to the financial information of components that are relevant to the identification and assessment of the risks of material misstatement of the group financial statements. (Ref: Para. A68)

24. In applying ISA 550,¹⁴ the group engagement team shall discuss with component auditors related party relationships or transactions identified by group management, and any other related parties of which the group engagement team is aware, that are relevant to the work of the component auditor. (Ref: Para. A69)

¹³ ISA 315 (Revised 2019), paragraph 19

¹⁴ ISA 550, *Related Parties*, paragraph 17

25. In applying ISA 570 (Revised),¹⁵ the group engagement team shall:
- (a) Discuss with component auditors any events or conditions identified by group management or the group engagement team, that may cast significant doubt on the component's ability to continue as a going concern; and
 - (b) Discuss with component auditors any events or conditions identified by group management or the group engagement team, that may cast significant doubt on the group's ability to continue as a going concern that is relevant to the work of the component auditor.

Materiality

26. In applying ISA 320¹⁶ and ISA 450,¹⁷ when classes of transactions, account balances or disclosures in the group financial statements are disaggregated across components for purposes of planning and performing audit procedures, the group engagement team shall determine:
- (a) Component performance materiality. Such amount shall be lower than group performance materiality to address aggregation risk. (Ref: Para. A70–A73)
 - (b) The threshold above which misstatements identified in component financial information are to be communicated to the group engagement team. Such threshold shall not exceed the amount regarded as clearly trivial to the group financial statements. (Ref: Para. A74)

Considerations When Component Auditors Are Involved

27. The group engagement team shall communicate to the component auditor:
- (a) Component performance materiality; and
 - (b) The threshold above which misstatements identified in the financial information of a component are to be communicated to the group engagement team.

Identifying and Assessing the Risks of Material Misstatement

28. In applying ISA 315 (Revised 2019),¹⁸ based on the understanding obtained in paragraph 22, the group engagement team shall take responsibility for the identification and the assessment of the risks of material misstatement of the group financial statements. (Ref: Para. A75–A80)

Considerations When Component Auditors Are Involved

29. When risk assessment procedures related to the identification and assessment of the risks of material misstatement of the group financial statements are assigned to component auditors, the group engagement team shall consider the results of the component auditors' work and determine whether it provides an appropriate basis for the identification and the assessment of the risks of material misstatement of the group financial statements. (Ref: Para. A81–A84)

¹⁵ ISA 570 (Revised), *Going Concern*

¹⁶ ISA 320, paragraph 11

¹⁷ ISA 450, *Evaluation of Misstatements Identified during the Audit*, paragraph 5

¹⁸ ISA 315 (Revised 2019), paragraph 28-29

Responding to the Assessed Risks of Material Misstatement

30. In applying ISA 330,¹⁹ the group engagement team shall take responsibility for the nature, timing and extent of further audit procedures to be performed. (Ref: Para. A85–A94)

Consolidation Process

31. The group engagement team shall take responsibility for designing and performing further audit procedures to respond to the assessed risks of material misstatement of the group financial statements arising from the consolidation process. This shall include:
- (a) Evaluating whether all entities and business units have been included in the group financial statements as required by the applicable financial reporting framework and, if applicable, to perform further audit procedures on sub-consolidations; and (Ref: Para. A95)
 - (b) Evaluating the appropriateness, completeness and accuracy of consolidation adjustments and reclassifications. (Ref: Para. A96)
32. If the financial information of an entity or business unit has not been prepared in accordance with the same accounting policies applied to the group financial statements, the group engagement team shall evaluate whether the financial information has been appropriately adjusted for purposes of preparing and presenting the group financial statements.
33. If the group financial statements include the financial statements of an entity or business unit with a financial reporting period-end that differs from that of the group, the group engagement team shall take responsibility for evaluating whether appropriate adjustments have been made to those financial statements in accordance with the applicable financial reporting framework.

Considerations When Component Auditors Are Involved

34. When the nature, timing and extent of further audit procedures to be performed is determined by component auditors, the group engagement team shall discuss with component auditors matters that are relevant to the design of responses to the assessed risks of material misstatement of the group financial statements. (Ref: Para. A97–A102)
35. If significant risks of material misstatement of the group financial statements have been identified in a component on which a component auditor is determining the further audit procedures to be performed, the group engagement team shall evaluate the appropriateness of those further audit procedures.

Consolidation Process

36. In accordance with paragraph 21, when component auditors perform further audit procedures on the consolidation process, including on sub-consolidations, the group engagement team shall determine the nature and extent of direction and supervision of component auditors and the review of their work. (Ref: Para. A103)
37. The group engagement team shall determine whether the financial information identified in the component auditor's communication (see paragraph 41(a)) is the financial information that is incorporated in the group financial statements.

¹⁹ ISA 330, paragraph 6-7

Related Parties

38. In applying ISA 550, the group engagement team shall request the component auditor to communicate on a timely basis related parties not previously identified by group management or the group engagement team.

Using Audit Evidence from an Audit Performed for Another Purpose

39. If an audit has been performed on the financial statements of an entity or business unit that is part of the group, and an auditor's report has been issued for statutory, regulatory or other reasons, and the group engagement team plans to use such work as audit evidence for the group audit, the group engagement team shall evaluate whether: (Ref: Para. A104–A106)
- (a) The audit procedures performed are an appropriate response to the assessed risks of material misstatement of the group financial statements;
 - (b) Performance materiality used for that audit is appropriate for the purposes of the group audit; and
 - (c) Other relevant requirements in this ISA have been met with respect to the use of the work of a component auditor, including the requirements in paragraphs 18 and 19.

Two-Way Communication Between the Group Engagement Team and the Component Auditor

40. The group engagement team shall communicate on a timely basis with component auditors. (Ref: Para. A107–A112)
41. The group engagement team shall request the component auditor to communicate matters relevant to the group engagement team's conclusion with regard to the group audit. Such communication shall include:
- (a) Identification of the financial information on which the component auditor is reporting;
 - (b) Information on instances of non-compliance with laws or regulations;
 - (c) Uncorrected misstatements of the financial information on which the component auditor performed further audit procedures (the list need not include misstatements that are below the threshold for clearly trivial misstatements communicated by the group engagement team);
 - (d) Indicators of possible management bias;
 - (e) Description of any identified deficiencies in the group's system of internal control;
 - (f) Other significant matters that the component auditor communicated or expects to communicate to those charged with governance of the component, including fraud or suspected fraud involving component management, employees who have significant roles in the group's system of internal control at the component level or others where the fraud resulted in a material misstatement of the financial information of the component;
 - (g) Any other matters that may be relevant to the group audit, or that the component auditor wishes to draw to the attention of the group engagement team, including exceptions noted in the written representations that the component auditor requested from component management; and
 - (h) The component auditor's overall findings, conclusions or opinion.

Evaluating Communications with Component Auditors

42. The group engagement team shall evaluate the communications with component auditors. In doing so, the group engagement team shall:
- (a) Discuss significant matters arising from that evaluation with the component auditor, component management or group management, as appropriate; and
 - (b) Determine how and the extent to which it is necessary to review parts of the component auditor's audit documentation. (Ref: Para. A113)
43. If the component auditor does not communicate the matters requested by the group engagement team, the group engagement team shall consider whether the information can be obtained through other sources. If such information cannot be obtained through other sources, the group engagement team shall consider the implications for the group audit, in accordance with paragraph 45.

Subsequent Events

44. In applying ISA 560,²⁰ the group engagement team shall take responsibility for performing procedures designed to identify events that may require adjustment to or disclosure in the group financial statements, including, as appropriate, requesting component auditors to perform procedures, for events that occur between the dates of the financial information of the components and the date of the auditor's report on the group financial statements. (Ref: Para. A114)

Evaluating the Sufficiency and Appropriateness of Audit Evidence Obtained

45. In applying ISA 330,²¹ the group engagement team shall evaluate whether sufficient appropriate audit evidence has been obtained from the audit procedures performed, including with respect to the work performed by component auditors, on which to base the group audit opinion. (Ref: Para. A115–A116)

Evaluating the Effect on the Group Audit Opinion

46. The group engagement partner shall evaluate the effect on the group audit opinion of any uncorrected misstatements (whether identified by the group engagement team or communicated by component auditors) and any instances where there has been an inability to obtain sufficient appropriate audit evidence. (Ref: Para. A117)

Considerations When Component Auditors Are Involved

47. If the group engagement team concludes that the work of the component auditor is insufficient, the group engagement team shall determine what additional procedures are to be performed, and whether they are to be performed by the component auditor or by the group engagement team.

Auditor's Report

48. The auditor's report on the group financial statements shall not refer to a component auditor, unless required by laws or regulations to include such reference. If such reference is required by laws or regulations, the auditor's report shall indicate that the reference does not diminish

²⁰ ISA 560, *Subsequent Events*, paragraph 7

²¹ ISA 330, paragraph 26

the group engagement partner's or the group engagement partner's firm's responsibility for the group audit opinion. (Ref: Para. A118–A119)

Communication with Group Management and Those Charged with Governance of the Group (Ref: Para. A120)

49. The group engagement team shall determine which identified deficiencies in internal control to communicate to those charged with governance of the group and group management in accordance with ISA 265.²² In making this determination, the group engagement team shall consider deficiencies in internal control that have been identified by the group engagement team or that have been communicated by component auditors.

Communication with Group Management

50. If fraud has been identified by the group engagement team or brought to its attention by a component auditor (see paragraph 41 (f)), or information indicates that a fraud may exist, the group engagement team shall communicate this on a timely basis to the appropriate level of group management in order to inform those with primary responsibility for the prevention and detection of fraud of matters relevant to their responsibilities. (Ref: Para. A121)
51. A component auditor may be required by statute, regulation or for another reason, to express an audit opinion on the financial statements of an entity or business unit that forms part of the group. In that case, the group engagement team shall request group management to inform management of the entity or business unit of any matter of which the group engagement team becomes aware that may be significant to the financial statements of the entity or business unit, but of which management of the entity or business unit may be unaware. If group management refuses to communicate the matter to component management, the group engagement team shall discuss the matter with those charged with governance of the group. If the matter remains unresolved, the group engagement team, subject to legal and professional confidentiality considerations, shall consider whether to advise the component auditor not to issue the auditor's report on the financial statements of the entity or business unit until the matter is resolved. (Ref: Para. A122)

Communication with Those Charged with Governance of the Group

52. The group engagement team shall communicate the following matters with those charged with governance of the group, in addition to those required by ISA 260 (Revised)²³ and other ISAs: (Ref: Para. A123)
- (a) An overview of the work to be performed at components and the nature of the group engagement team's planned involvement in the work to be performed by component auditors.
 - (b) Instances where the group engagement team's evaluation of the work of a component auditor gave rise to a concern about the quality of that component auditor's work, and how the group engagement team addressed the concern.
 - (c) Any limitations on the group audit, for example, where the access to information or people may have been restricted.
 - (d) Fraud or suspected fraud involving group management, component management,

²² ISA 265, *Communicating Deficiencies in Internal Control to Those Charged with Governance and Management*

²³ ISA 260 (Revised), *Communication with Those Charged with Governance*

employees who have significant roles in the group's system of internal control or others where the fraud resulted in a material misstatement of the group financial statements.

Documentation

53. In applying ISA 230,²⁴ the group engagement team shall include in the audit documentation: (Ref: Para A124, A129–A130)
- (a) Significant matters related to restrictions on access to people or information that were considered before deciding to accept or continue the engagement, or that arose subsequent to acceptance or continuance, and how such matters were addressed.
 - (b) The determination of component performance materiality and the threshold for communicating misstatements in component financial information to the group engagement team.
 - (c) The nature, timing and extent of the group engagement team's direction and supervision of component auditors and the review of their work. (Ref: Para. A125–A128)
 - (d) Matters related to communication with component auditors, including:
 - (i) The matters required to be discussed in accordance with paragraphs 24–25 and 38.
 - (ii) Matters relevant to the group engagement team's conclusion with regard to the group audit, as required by paragraph 41.
 - (e) The group engagement team's evaluation of, and response to, findings of the component auditors with respect to matters that could have a material effect on the group financial statements.

* * *

Application and Other Explanatory Material

Scope (Ref: Para. 1–2)

- A1. This proposed ISA deals with the special considerations for the group engagement partner and group engagement team in applying the requirements and guidance in proposed ISA 220 (Revised), including with respect to the direction and supervision of component auditors and the review of their work.
- A2. Proposed ISQM 1²⁵ addresses the engagements for which an engagement quality review is required to be performed. Proposed ISQM 2²⁶ deals with the appointment and eligibility of the engagement quality reviewer and the engagement quality reviewer's responsibilities relating to performing and documenting an engagement quality review, including for a group audit.
- A3. This proposed ISA applies when the auditor has been engaged to audit group financial

²⁴ ISA 230, *Audit Documentation*, paragraphs 8–11 and A6

²⁵ Proposed International Standard on Quality Management (ISQM) 1, *Quality Management for Firms that Perform Audits or Reviews of Financial Statements, or Other Assurance or Related Services Engagements*. All References to proposed ISQM 1 are to the version presented to the IAASB in March 2020.

²⁶ Proposed ISQM 2, *Engagement Quality Reviews*. All References to proposed ISQM 2 are to the version presented to the IAASB in March 2020.

statements. Group financial statements, as defined, include the financial information of more than one entity or business unit. A key factor in determining whether financial statements are group financial statements is whether financial information is prepared through a consolidation process as described in paragraphs 9 and A12-A14.

- A4. An entity or business unit of a group may also prepare group financial statements that incorporate the financial information of those entities or business units it encompasses (that is, a subgroup). This ISA therefore applies to such subgroups.
- A5. When this ISA applies, the auditor determines an appropriate approach to planning and performing audit procedures to respond to the assessed risks of material misstatement of the group financial statements. For this purpose, the group engagement team uses judgment in determining the components for which audit procedures will be performed. The manner in which components are viewed for purposes of planning and performing a group audit may be influenced by the group structure, but may or may not be aligned with the way in which the group is organized, which could be, for example, by legal entities, geographic locations, or lines of business.
- A6. For example, for a group comprised of 15 legal entities that are required to be consolidated under the provisions of the applicable financial reporting framework (i.e., group financial statements), the auditor may plan and perform the group audit by combining these 15 entities into three components based on the commonality of information systems and internal control.

Involvement of Component Auditors (Ref: Para. 3)

- A7. The involvement of component auditors may be necessary for various reasons. For example, when the group has many components across multiple jurisdictions, the group engagement team may need the assistance of component auditors to identify, assess and respond to the risks of material misstatement of the group financial statements.
- A8. The group engagement team may decide to assign certain audit procedures to, or obtain information from, component auditors to fulfill the requirements of this ISA. For example, when obtaining an understanding of the entity and its environment for a continuing group audit in accordance with paragraph 22 of this ISA, the group engagement team may discuss with a component auditor whether there are any significant changes in the business of the component that could have an effect on the risks of material misstatement of the group financial statements.

Definitions

Aggregation Risk (Ref: Para. 7(a))

- A9. Aggregation risk exists in all audits of financial statements, but is particularly important to understand and address in a group audit engagement because there is a greater likelihood that audit procedures will be performed on classes of transactions, account balances or disclosures that are disaggregated across components.

Component Auditor (Ref: Para. 7(c))

- A10. References in this ISA to the engagement team include members of the group engagement team and component auditors. The engagement team includes individuals from the group engagement team's firm and may include individuals from a network firm, a firm that is not a network firm, or an external service provider.

A11. In some circumstances, the group engagement team may perform centralized testing on account balances, classes of transactions or disclosures, or may perform audit procedures related to a component. In these circumstances, the group engagement team is not considered a component auditor for purposes of this ISA.

Consolidation Process (Ref: Para. 9)

A12. The requirements for the preparation and presentation of the group financial statements may be specified in the applicable financial reporting framework, which may therefore affect the determination of the financial information of entities or business units to be included in the group financial statements. For example, some frameworks require the preparation of consolidated financial statements when an entity (a parent entity) controls one or more other entities (e.g., subsidiaries) through majority ownership interest or other means. In some cases, the applicable financial reporting framework includes separate requirements for, or may otherwise allow, the presentation of combined financial statements for entities that have no parent but are under common control.

A13. When branches or divisions within a single entity prepare financial information, through separate branch or divisional accounting, financial reporting frameworks may require the financial information of the branches or divisions to be aggregated into the financial statements of the entity, including the elimination of interbranch or interdivisional transactions and balances. In some circumstances, the accounting for the branches or divisions may be performed centrally, and there is no separately prepared financial information for the branches or divisions that requires aggregation. In these circumstances, unless there are other entities or business units whose financial information is subject to a consolidation process as described in paragraph 9, the financial statements do not represent group financial statements and therefore this proposed ISA does not apply.

A14. The detailed aspects of the consolidation process vary from one group to another, depending on the group's structure and information system, including the financial reporting process. However, a consolidation process involves certain considerations, such as the elimination of intragroup transactions and balances and, when applicable, implications of different reporting periods for entities or business units included in the group financial statements.

Leadership Responsibilities for Managing and Achieving Quality on a Group Audit (Ref: Para. 10)

A15. It may be not possible or practical for the group engagement partner to solely deal with all requirements in proposed ISA 220 (Revised), particularly when the engagement team includes a large number of component auditors located in multiple locations. In managing quality at the engagement level, proposed ISA 220 (Revised)²⁷ allows the engagement partner to assign responsibilities for the design or performance of procedures, tasks, or other actions to appropriately skilled or suitable experienced members of the engagement team to assist the engagement partner. Accordingly, the group engagement partner may assign responsibilities to other members of the engagement team and these members may assign responsibilities further. In such circumstances, proposed ISA 220 (Revised) requires that the engagement partner shall continue to take overall responsibility for managing and achieving quality on the engagement.²⁸

²⁷ Proposed ISA 220 (Revised), paragraph 15

²⁸ Proposed ISA 220 (Revised), paragraph 15

A16. Policies or procedures established by the firm, or that are common network requirements or network services, may support the group engagement partner by facilitating communication between the group engagement team and component auditors from that network and supporting the group engagement team's direction and supervision of those component auditors and the review of their work.

Acceptance and Continuance

Determining Whether Sufficient and Appropriate Audit Evidence Can Reasonably Be Expected To be Obtained (Ref: Para. 11–12)

A17. In determining whether sufficient appropriate audit evidence can reasonably be expected to be obtained the group engagement team may obtain an understanding of matters such as:

- The group structure, including both the legal and organizational structure.
- Business activities that are significant to the group, including the industry and regulatory, economic and political environments in which those activities take place.
- The use of service organizations.
- The use of shared service centers.
- The consolidation process.
- Whether the group engagement team:
 - Will have unrestricted access to those charged with governance of the group, group management, those charged with governance of the component, component management, component information; and
 - Will be able to perform necessary work on the financial information of the components.

A18. In the case of a new engagement, the group engagement team's understanding of the matters in paragraph A17 may be obtained from:

- Information provided by group management;
- Communication with group management;
- Communication with those charged with governance of the group; and
- Where applicable, communication with component management or the previous group engagement team.

A19. For a continuing engagement, obtaining audit evidence may be affected by significant changes, for example:

- Changes in the group structure (e.g., acquisitions, disposals, reorganizations, or changes in how the group financial reporting system is organized).
- Changes in components' business activities that are significant to the group.
- Changes in the composition of those charged with governance of the group, group management, or key management of components for which audit procedures are expected to be performed.
- Concerns the group engagement team has with regard to the integrity and competence of group or component management.

- Changes in the applicable financial reporting framework.
- A20. There may be more complexities with obtaining sufficient appropriate audit evidence in a group audit with components in jurisdictions other than the group engagement team's jurisdiction because of cultural and translation issues and different laws or regulations (e.g., regulations restricting access to data).
- A21. Restrictions may be imposed after the group engagement partner's acceptance of the group audit engagement that may affect the engagement team's ability to obtain sufficient appropriate audit evidence. Such restrictions may include those affecting:
- The group engagement team's access to component information, management or those charged with governance of components, or the component auditors (including relevant audit documentation sought by the group engagement team); or
 - The work to be performed on the financial information of components.

In exceptional circumstances, such restrictions may lead to withdrawal from the engagement, where withdrawal is possible under applicable laws or regulations. In addition, an inability to obtain sufficient appropriate audit evidence would need to be evaluated, in accordance with ISA 705 (Revised),²⁹ in forming an opinion on the group financial statements.

Agreeing the Terms of Audit Engagements (Ref: Para. 13)

- A22. ISA 210 requires the auditor to agree the terms of engagement with management or those charged with governance.³⁰ The terms of engagement identify the applicable financial reporting framework.³¹ Additional matters may be included in the terms of a group audit engagement, such as:
- The communication between the group engagement team and component auditors should be unrestricted to the extent possible under laws or regulations;
 - Important communications between component auditors and those charged with governance of the component or component management, including communications on significant deficiencies in internal control, should be communicated to the group engagement team;
 - Important communications between regulatory authorities and components related to financial reporting matters should be communicated to the group engagement team; and
 - The group engagement team should be permitted to perform work or request a component auditor to perform work at the component.
- A23. If the group engagement team cannot obtain the agreement of group management that it acknowledges and understands its responsibilities in accordance with paragraph 13, the group engagement team is required to not accept the group audit engagement, unless required by laws or regulations to do so.³²

²⁹ ISA 705 (Revised), *Modifications to the Opinion in the Independent Auditor's Report*

³⁰ ISA 210, paragraph 9

³¹ ISA 210, paragraph 8

³² ISA 210, paragraph 8

Restrictions on Access to Information or People (Ref: Para. 14–15)

- A24. Restrictions on access to information or people do not alleviate the requirement for the group engagement team to obtain sufficient appropriate audit evidence.
- A25. Access to information or people can be restricted for many reasons, such as restrictions imposed by management, local laws or regulations or other conditions, for example, war, civil unrest or outbreaks of disease.
- A26. In many cases, the group engagement team may be able to overcome restrictions on access to information or people, for example:
- When laws or regulations restrict sending relevant audit documentation across borders, the group engagement team may be able to access the relevant audit documentation by:
 - Visiting the location of the component;
 - Reviewing the relevant audit documentation remotely with the use of technology, where not prohibited by laws or regulations;
 - Discussing the procedures performed by the component auditor; or
 - Discussing with management the need to communicate with regulators.
 - When the group has a non-controlling interest in an entity that is accounted for by the equity method, the group engagement team may be able to overcome restrictions by:
 - Determining whether provisions exist (e.g., in the terms of joint venture agreements, or the terms of other investment agreements) regarding access by the group to the financial information of the entity, and requesting management to exercise such rights;
 - Considering financial information that is available from group management, as group management also needs to obtain the entity's financial information in order to prepare the group financial statements;
 - Considering publicly available information, such as audited financial statements, public disclosure documents, or quoted prices of equity instruments in the associate; or
 - Considering other sources of information that may corroborate or otherwise contribute to audit evidence obtained. For example, if the group has representatives who are on the executive board or are members of those charged with governance of the associate, discussion with them regarding the associate and its operations and financial status may be a useful source of information.
 - When war, other unrest or outbreaks of disease restricts access to relevant audit documentation of a component auditor, the group engagement team may be able to meet with the component auditor in a location different from where the component auditor is located or review the relevant audit documentation remotely with the use of technology, where not prohibited by laws or regulations.
 - When access to component management or those charged with governance of the component is restricted, the group engagement team may be able to perform the work themselves by working with group management or those charged with governance of the group.

- A27. When the group engagement team cannot overcome restrictions, the group engagement team's firm may communicate with regulators, listing authorities, or others, about the restrictions (e.g., the group engagement team's firm may ask a listing authority for a different filing date) and encourage group management to communicate with regulators. This may be particularly useful when restrictions affect multiple audits in the jurisdiction or by the same firm, for example, because of war, civil unrest or outbreaks of disease in a major economy.
- A28. Restrictions on access may have other implications for the group audit. For example, if restrictions are imposed by group management, the group engagement team may need to reconsider the reliability of group management's responses to the group engagement team's inquiries and may call into question group management's integrity.

Effect of Restrictions on the Auditor's Report on Group Financial Statements

- A29. When the group engagement team is unable to obtain sufficient appropriate audit evidence, the considerations in ISA 705 (Revised) apply. Appendix 1 contains an example of an auditor's report containing a qualified group audit opinion based on the group engagement team's inability to obtain sufficient appropriate audit evidence in relation to a component that is accounted for by the equity method.

Laws or Regulations Prohibit the Group Engagement Partner from Declining or Withdrawing from an Engagement

- A30. Laws or regulations may prohibit the group engagement partner from declining or withdrawing from an engagement. For example, in some jurisdictions the auditor is appointed for a specified period of time and is prohibited from withdrawing before the end of that period. Also, in the public sector, the option of declining or withdrawing from an engagement may not be available to the auditor due to the nature of the mandate or public interest considerations. In these circumstances, the requirements in this ISA still apply to the group audit, and the effect of the group engagement team's inability to obtain sufficient appropriate audit evidence is addressed in ISA 705 (Revised).

Consideration When Component Auditors Are Involved (Ref: Para. 16)

- A31. In evaluating whether the group engagement team will be able to be involved in the work of the component auditor to the extent necessary, the group engagement team may obtain an understanding of whether the engagement team will have unrestricted access to the component auditor, including relevant audit documentation sought by the group engagement team (e.g., audit evidence related to components located in a different jurisdiction may be in a foreign language and may need to be translated for use by the group engagement team).

Relevant Ethical Requirements (Ref: Para. 18)

- A32. When performing work at a component for a group audit engagement, the component auditor is subject to ethical requirements, including those relating to independence, that are relevant to the group audit. Such requirements may be different or in addition to those applying to the component auditor when performing an audit on the financial statements of an entity or business unit that is part of the group for statutory, regulatory or other reasons in the component auditor's jurisdiction.
- A33. The group engagement team may need to communicate relevant ethical requirements, including those related to independence, to all component auditors. In doing so, the group engagement team may consider whether additional information or training for component

auditors is necessary with respect to the provisions of the ethical requirements that are relevant to the group audit engagement.

- A34. Proposed ISA 220 (Revised) requires the engagement partner to remain alert throughout the audit engagement, through observation and making inquiries as necessary, for actual or suspected breaches of relevant ethical requirements by the engagement team.³³ Becoming aware of actual or suspected breaches of relevant ethical requirements may be more challenging for a group audit, particularly where component auditors are not subject to common network services or network requirements in respect of relevant ethical requirements. In such circumstances, the group engagement team may instruct component auditors to communicate relevant information to the group engagement partner when actual or suspected breaches by component auditors may have occurred.

Engagement Resources (Ref: Para. 19)

- A35. The determination whether sufficient and appropriate resources to perform the engagement are assigned or made available to the engagement team may be more challenging in a group audit engagement. Audit work may be conducted across different locations with different characteristics (e.g., different languages, time zones and cultures) where collaboration is more challenging, and when component auditors are from different firms that do not have common systems of quality management. For example, a component auditor may determine that the work of an auditor's expert is needed in relation to an account balance at the component that is a significant account balance to the group financial statements. In such circumstances, the group engagement team may wish to discuss the qualifications of the auditor's expert with the component auditor to evaluate whether the auditor's expert has the necessary expertise and objectivity. If the group engagement partner is unable to determine whether the auditor's expert has the necessary expertise and objectivity, the group engagement team may need to seek another expert with the appropriate expertise and objectivity or change the planned approach to the nature, timing and extent of direction and supervision of component auditors and the review of their work.

Competence and capabilities of the component auditors (Ref: Para. 19(a))

- A36. Determining whether the component auditor has the appropriate competence and capabilities influences the nature, timing and extent of the engagement partner's direction and supervision of the component auditor and the review of their work. Determining whether the component auditor has the appropriate competence and capabilities is a matter of professional judgment and is influenced by the nature and circumstances of the group audit engagement.
- A37. In determining whether component auditors have the appropriate competence and capabilities to perform the necessary procedures at the component for purposes of the group audit, the group engagement partner may consider matters such as:
- Previous experience with or knowledge of the component auditor.
 - The component auditor's specialized skills (e.g., industry specific knowledge).
 - The component auditor's understanding of the applicable financial reporting framework relevant to the group financial statements, and any instructions provided by group management.

³³ Proposed ISA 220 (Revised), paragraph 19

- The degree to which the group engagement team and component auditor are subject to common systems of quality management, for example, whether the group engagement team and a component auditor:
 - Use common resources to perform the work (e.g., audit methodologies or information technology (IT) applications);
 - Share common policies or procedures affecting the engagement performance (e.g., direction and supervision and review of work or consultation);
 - Are subject to common monitoring activities; or
 - Have other commonalities, including common leadership or a common cultural environment.
 - The consistency or similarity of:
 - Laws or regulations or legal system;
 - Language and culture;
 - Education and training;
 - Professional oversight, discipline, and external quality assurance; or
 - Professional organizations and standards.
 - Information obtained through interactions with component management, those charged with governance, and other key personnel, such as internal auditors.
- A38. The procedures to determine the component auditor's competency and capability may include, for example:
- An evaluation of the information communicated by the group engagement team's firm to the group engagement team, including:
 - The firm's ongoing communication related to monitoring and remediation, in circumstances when the group engagement team and component auditor are from the same firm.³⁴
 - Information from the network about the results of the monitoring activities undertaken by the network across the network firms.
 - Discussing the matters in paragraph A47 with the component auditor.
 - Requesting the component auditor to confirm the matters referred to in paragraph 18 in writing.
 - Discussing the component auditor's competency and capabilities with colleagues in the group engagement partner's firm, or with a reputable third party that has knowledge of the component auditor.
 - Obtaining confirmations from the professional body or bodies to which the component auditor belongs, the authorities by which the component auditor is licensed, published external inspection reports, or other third parties. In subsequent years, requesting that the component auditor confirm whether anything in relation to the matters listed in paragraph 19(a)–(b) has changed since the previous year.

³⁴ Proposed ISQM 1, paragraph 53

- A39. The engagement partner's firm and the component auditor's firm may be members of the same network and may be subject to common network requirements or use common networks services.³⁵ When determining whether component auditors have the appropriate competence and capabilities to perform work in support of the group audit engagement, the group engagement partner may be able to depend on such network requirements, for example, those addressing professional training, or recruitment or that require the use of audit methodologies and related implementation tools. In accordance with proposed ISQM 1, the firm is responsible for designing, implementing and operating its system of quality management, and the firm may need to adapt or supplement network requirements or network services to be appropriate for use in its system of quality management, taking into account the nature and circumstances of the firm and the engagements it performs.
- A40. Working with component auditors that are not from the same firm may be different than working with individuals from the same firm. For example, the group engagement team and component auditors may work in different countries with different languages, culture, business and market conditions. Also, different firms may have different systems of quality management, and the skills and experience of the group engagement team with respect to the group audit may differ from those of the component auditors. These differences may pose challenges in the coordination of the overall audit strategy and audit plan between the group engagement team and component auditors. Adequate and timely involvement by the group engagement partner and group engagement team may address these challenges.

Automated tools or techniques

- A41. As described in proposed ISA 220 (Revised),³⁶ when determining whether the engagement team has the appropriate competence and capabilities, the group engagement partner may take into consideration such matters as the expertise of the component auditor in the use of automated tools or techniques. When component auditors use automated tools and techniques, the group engagement team may include in communications with component auditors that the use of such automated tools and techniques need to comply with the group engagement team's instructions. The group engagement team may also request component auditors to confirm that they have complied with the group engagement team's instructions.

Monitoring and remediation (Ref: Para. 19(b))

- A42. If the group engagement team and the component auditor are members of the same network and are subject to common monitoring activities undertaken by the network across network firms' systems of quality management, the results of the network's monitoring activities may include findings or deficiencies in relation to the component auditor's firm that may be relevant to the group engagement team's understanding of the competence and capability of the component auditor, if sufficiently detailed. The group engagement team may obtain such information through the group engagement team's firm or, if the group engagement team's firm does not provide such information, from the component auditor. This information influences the nature, timing and extent of the engagement partner's direction and supervision of the component auditor and the review of their work.
- A43. When the group engagement team cannot obtain information about the results of the monitoring and remediation process with respect to the component auditor's firm, the group engagement team may be able to obtain information through other sources, for example, the

³⁵ Proposed ISQM 1, paragraph 58 and 59

³⁶ Proposed ISA 220 (Revised), paragraph A20

group engagement team firm's network may provide aggregated information about the monitoring activities undertaken by the network for the firms within the network that includes the component auditor's firm.

Application of the Group Engagement Team's Understanding of a Component Auditor (Ref: Para. 20)

- A44. The group engagement team cannot overcome the fact that a component auditor is not independent by being involved in the work of the component auditor or by supplementing the work of component auditor by performing additional risk assessment or further audit procedures on the financial information of the component.
- A45. However, the group engagement team may be able to overcome less than serious concerns about the component auditor's professional competency (e.g., lack of industry specific knowledge), or the fact that the component auditor does not operate in an environment that actively oversees auditors, by being more involved in the work of the component auditor or by directly performing further audit procedures on the financial information of the component.

Engagement Performance (Ref: Para. 21)

- A46. The group engagement partner is responsible for the nature, timing and extent of direction and supervision of the members of the engagement team and the review of their work.³⁷ However, as described in paragraph A15, it may be not possible or practical for the group engagement partner to solely determine the nature, timing and extent of direction, supervision and review, particularly when the engagement team includes a large number of component auditors that may be located in multiple locations. In managing quality at the engagement level, the group engagement partner may assign such responsibilities to other members of the engagement team and these members may assign responsibilities further.
- A47. The nature timing and extent of direction and supervision and review of their work may be tailored taking into account the nature and circumstances of the engagement and, for example:
- The assessed risks of material misstatement. For example, if the group engagement team has identified a component that is likely to include significant risks, a corresponding increase in the extent of direction and supervision of the component auditor and a more detailed review of the component auditor's audit documentation may be appropriate.
 - The competence and capabilities of the component auditors performing the audit work. For example, if the group engagement team has no previous experience working with a component auditor, the group engagement team may communicate more detailed instructions or introduce greater in-person supervision of the component auditor as the work is performed.
 - The location of engagement team members, including the extent to which engagement team members are dispersed across multiple locations, including where service delivery centers are used. For example, direction and supervision of individuals located at service delivery centers and the review of their work may need to be more formalized and structured than when members of the engagement team are all situated in the same location.

³⁷ Proposed ISA 220 (Revised), paragraph 29

- Access to component auditors' working papers. For example, where component auditor working papers cannot be transferred out of the jurisdiction, greater in-person supervision of the component auditor and in-person or electronic review of the component auditor's audit documentation may be appropriate (see also paragraphs A24–A29).
- A48. There are different ways in which the group engagement partner may direct and supervise component auditors and review their work, for example:
- Meetings or calls with component auditors to communicate identified and assessed risk, issues, findings and conclusions.
 - Reviews of the component auditor's documentation in person or through the use of technology or automated tools and techniques.
 - Participating in the closing and other key meetings between the component auditors and component management.

Understanding the Group and Its Environment, the Applicable Financial Reporting Framework and the Group's System of Internal Control (Ref: Para. 22)

- A49. ISA 315 (Revised 2019) contains requirements and guidance on matters the auditor may consider when obtaining an understanding of the entity and its environment, the applicable financial reporting framework, and the entity's system of internal control.³⁸ Appendix 2 of this ISA provides further explanation of the components of the group's system of internal control, including controls over the group's financial reporting process and the consolidation process.
- A50. The entity's information system and financial reporting process may be closely aligned with the organizational structure, for example, a parent and one or more subsidiaries, joint ventures, or investees accounted for by the equity method; a head office and one or more divisions or branches; or a combination of both. Some groups, however, may organize their information system by function, process, product or service (or by groups of products or services), or geographic locations. In these cases, the entity or business unit for which group or component management prepares financial information that is included in the group financial statements may be a function, process, product or service (or group of products or services), or geographic location.
- A51. The group engagement team's understanding of the group and its environment, the applicable financial reporting framework, and the group's system of internal control may be obtained through communications with:
- Group management or component management, including those who have knowledge of the group's system of internal control, accounting policies and practices, and the consolidation process;
 - Component auditors; or
 - Auditors that perform an audit for statutory, regulatory or another reason on the financial statements of an entity or business unit that is part of the group.

³⁸ ISA 315 (Revised 2019), paragraphs A50-A89

The Group and Its Environment (Ref: Para. 22(a))

A52. An understanding of the group's organizational structure and its business model may enable the group engagement team to understand such matters as:

- The complexity of the group's structure. A group may be more complex than a single entity because a group may have several subsidiaries, divisions or other business units, including in multiple locations. Also, a group's legal structure may be different from the operating structure, for example, for tax purposes. Complex structures often introduce factors that may give rise to increased susceptibility to risks of material misstatement such as whether goodwill, joint ventures or special purpose entities are accounted for appropriately and whether adequate disclosures have been made.
- The geographic locations of the group's operations. Having a group that is located in multiple geographical locations may give rise to increased susceptibility to risks of material misstatement. For example, certain geographical locations may involve different languages, cultures and business practices.
- The structure and complexity of the group's IT environment. A complex IT environment often introduces factors that may give rise to increased susceptibility to risks of material misstatement. For example, a group may have a complex IT environment because of multiple IT systems that are not integrated due to recent acquisitions or mergers. Given that there may be multiple IT systems that are not integrated, it may be particularly important to obtain an understanding of the complexity of the security over the IT environment, including vulnerability of the IT applications, databases, and other aspects of the IT environment. A group may also use one or more external service providers for aspects of its IT environment.
- Relevant regulatory factors, including the regulatory environment. Different laws or regulations may introduce factors that may give rise to increased susceptibility to risks of material misstatement. A group may have operations that are subject to a high degree of complex laws or regulations in multiple jurisdictions, or entities or business units in the group that operate in multiple industries that are subject to different types of laws or regulations.
- The ownership, and relationships between owners and other people or entities, including related parties. Understanding the ownership and relationships can be more complex in a group that operates over multiple jurisdictions and when there are changes in ownership through formation, acquisition or joint ventures. These factors may give rise to increased susceptibility of risks of material misstatement.

A53. Obtaining an understanding of the similarities of the group's activities and business lines may enable the group engagement team to identify similar risks of material misstatement across components and design an appropriate response.

A54. The financial results of entities or business units are ordinarily measured and reviewed by group management. Inquiries of group management may reveal that group management relies on certain key indicators to evaluate the financial performance of the group's entities and business units and take action. The group engagement team's understanding of such performance measures may help to identify:

- Areas where there is increased susceptibility to the risk of material misstatement (e.g., due to pressures on component management to meet certain performance measures).
- Controls over the group's financial reporting process.

The Group's System of Internal Control

The Nature and Extent of Commonality of Controls (Ref: Para. 22(c)(i))

- A55. Group management may design controls that are intended to operate in a common manner across multiple entities or business units (i.e., common controls). For example, group management may design common controls for inventory management, that operate using the same IT system and that are implemented across all entities or business units in the group. Common controls may exist in each component of the group's system of internal control, and they may be implemented at different levels within the group (e.g., at the level of the consolidated group as a whole, or for other levels of aggregation within the group). Common controls may be direct controls or indirect controls. Direct controls are controls that are precise enough to address risks of material misstatement at the assertion level. Indirect controls are controls that support direct controls.³⁹
- A56. The understanding of the components of the group's system of internal control therefore includes understanding the commonality of the controls within those components across the group. When the group engagement team plans to test the operating effectiveness of identified controls⁴⁰ that are common across the group, the group engagement team evaluates the design and determines the implementation of those controls in accordance with ISA 315 (Revised 2019).
- A57. To determine the commonality of an identified control across the group, the group engagement team may consider whether:
- The control is designed centrally and required to be implemented as designed (i.e., without modification) at some or all components;
 - The control is implemented and, if applicable, monitored by individuals with similar responsibilities and capabilities at all the components where the control is implemented;
 - If a control uses information from IT applications, the IT applications and other aspect of the IT environment that generate the information are the same across the components or locations; or
 - If the control is automated, it is configured in the same way in each IT application across the components.
- A58. Judgment may often be needed to determine whether an identified control is a common control. For example, group management may require that all entities and business units perform a monthly evaluation of the aging of customers' accounts that are generated from a specific IT application. When the aging reports are generated from different IT infrastructures or the implementation of the IT application differs across entities or business units, the group engagement team may need to consider whether the control can still be determined to be common. This is because of differences in the design of the control that may exist due to the existence of different IT infrastructures (e.g., whether the IT application is configured in the same manner across different IT infrastructures, and whether there are effective general IT controls across different IT implementations of IT applications or different IT infrastructures).

³⁹ ISA 315 (Revised 2019), paragraph A5

⁴⁰ ISA 315 (Revised 2019), paragraph 26(a)

- A59. ISA 315 (Revised 2019)⁴¹ recognizes that, in some cases, an entity may use common IT processes across its IT environment or across certain IT applications or IT infrastructures, in which case common risks arising from the use of IT and common general IT controls may be identified.
- A60. Consideration of the level at which controls are performed within the group (e.g., at the level of the consolidated group as a whole or for other levels of aggregation within the group) and the degree of centralization and commonality may be important to the understanding of how information is processed and controlled. In some circumstances, controls may be performed centrally (e.g., performed only at a single entity or business unit), but may have a pervasive effect on other entities or business units (e.g., a shared services center that processes transactions on behalf of other entities or business units within the group). Typically, the processing of transactions and related controls at a shared service center operate in the same way for all transactions regardless of the entity or business unit (e.g., the processes, risks, and controls for all transactions, regardless of the source of the transaction, are the same). In such cases, it may be appropriate to identify the controls and evaluate the design and determine implementation of the controls, and if applicable test operating effectiveness, as a single population.

Centralized Activities (Ref: Para. 22(c)(ii))

- A61. Group management may centralize some of its activities, for example financial reporting or accounting functions may be performed for a particular group of common transactions or other financial information in a consistent and centralized manner for multiple entities or business units in a single location (e.g., where the initiation, authorization, recording, processing, or reporting of revenue transactions is performed at a shared service center).
- A62. Obtaining an understanding of how centralized activities fit into the overall group structure, and the nature of the activities undertaken, may help the group engagement team to identify and assess risks of material misstatement and appropriately respond to such risks. For example, controls at a shared service center may operate independently from other controls, or they may be dependent upon controls at an entity or business unit from which financial information is derived (e.g., sales transactions may be initiated and authorized at a component, but the processing may occur at the shared service center).

Communications About Significant Matters That Support the Preparation of the Group Financial Statements (Ref: Para. 22(c)(iv))

- A63. Group entities or business units may use a financial reporting framework for statutory, regulatory or another reason that is different from the financial reporting framework used for the group's financial statements. In such circumstances, an understanding of group management's financial reporting processes to align accounting policies and, where relevant, financial reporting period-ends that differ from that of the group, enables the group engagement team to understand how adjustments, reconciliations and reclassifications are made, and whether they are made centrally by group management or by the entity or business unit.

⁴¹ ISA 315 (Revised 2019), appendix 5, paragraph 21

Instructions by Group Management to Entities or Business Units

A64. In applying ISA 315 (Revised 2019),⁴² the group engagement team is required to understand how group management communicates significant matters that support the preparation of the group financial statements. To achieve uniformity and comparability of financial information, group management may issue instructions (i.e. communicate financial reporting policies) to the entities or business units that include details about financial reporting processes. Obtaining an understanding of group management's instructions may affect the group engagement team's identification and assessment of the risks of material misstatement of the group financial statements. For example, inadequate instructions may increase the likelihood of misstatements due to the risk that transactions are incorrectly recorded or processed, or that accounting policies are incorrectly applied.

A65. The group engagement team's understanding of the instructions may include the following:

- The clarity and practicality of the instructions for completing the reporting package.
- Whether the instructions:
 - Adequately describe the characteristics of the applicable financial reporting framework and the accounting policies to be applied;
 - Address information necessary to prepare disclosures that are sufficient to comply with the requirements of the applicable financial reporting framework, for example, disclosure of related party relationships and transactions, and segment information;
 - Address information necessary for making consolidation adjustments, for example, intra-group transactions and unrealized profits, and intra-group account balances; and
 - Include a reporting timetable.

Engagement Team Discussion (Ref: Para. 22)

A66. The group engagement partner's determination of which members of the engagement team to include in the discussions and the topics to be discussed, is affected by factors such as initial expectations about the risks of material misstatement and the expected involvement of component auditors.

A67. The discussions provide an opportunity to:

- Share knowledge of the components and their environments, including which components' activities are centralized.
- Exchange information about the business risks of the components or the group, and how inherent risk factors may affect susceptibility to misstatement of classes of transactions, account balances and disclosures.
- Exchange ideas about how and where the group financial statements may be susceptible to material misstatement due to fraud or error.
- Identify policies followed by group or component management that may be biased or designed to manage earnings that could lead to fraudulent financial reporting, for

⁴² ISA 315 (Revised 2019), paragraph 25(b)

example, revenue recognition practices that do not comply with the applicable financial reporting framework.

- Consider known external and internal factors affecting the group that may create an incentive or pressure for group management, component management, or others to commit fraud, provide the opportunity for fraud to be perpetrated, or indicate a culture or environment that enables group management, component management, or others to rationalize committing fraud.
- Consider the risk that group or component management may override controls.
- Consider whether uniform accounting policies are used to prepare the financial information of the components for the group financial statements and, where not, how differences in accounting policies are identified and adjusted (where required by the applicable financial reporting framework).
- Discuss fraud that has been identified in components, or information that indicates existence of a fraud in a component.
- Share information about risks of material misstatement of the financial information of a component that may apply more broadly to some, or all, of the other components.
- Share information that may indicate non-compliance with national laws or regulations, for example, payments of bribes and improper transfer pricing practices.
- Identify risks of material misstatement relevant to components where the exercise of professional skepticism may be particularly important.
- Discuss any events or conditions identified by group management, or the engagement team, that may cast significant doubt on the group's ability to continue as a going concern.
- Discuss related party relationships or transactions identified by group management, and any other related parties of which the engagement team is aware.

Considerations When Component Auditors are Involved (Ref: Para. 23)

A68. Factors that influence the group engagement team's decision about the nature and extent of risk assessment procedures assigned to component auditors include, for example:

- The number and geographical location of components;
- The nature of the components' business activities, including their complexity or specialization of operations; and
- The group's system of internal control, including the information system in place at the component.

Previous experience with the component auditor may also influence the group engagement team's decision whether to involve them in performing risk assessment procedures. When risk assessment procedures are assigned to component auditors, the group engagement team remains responsible for having an understanding of the group and its environment, the applicable financial reporting framework and the group's system of internal control.

Related Parties (Ref: Para. 24)

A69. The nature of related party relationships and transactions may, in some circumstances, give rise to higher risks of material misstatement of the financial statements than transactions with unrelated parties.⁴³ In a group audit there may be a higher risk of material misstatement of the group financial statements, including due to fraud, associated with related party relationships when:

- The group structure is complex;
- The group's information systems are not integrated and therefore less effective in identifying and recording related party relationships and transactions; and
- There are numerous or frequent related party transactions between entities and business units.

Planning and performing the audit with professional skepticism as required by ISA 200,⁴⁴ is therefore particularly important when these circumstances exist.

Materiality (Ref: Para. 26–27)

A70. A different component performance materiality may be established for each of the components where audit procedures are performed on financial information that is disaggregated. The component performance materiality amount for an individual component need not be an arithmetical portion of the group performance materiality and, consequently, the aggregate of component performance materiality amounts may exceed group performance materiality.

A71. ISA 320 requires the auditor to determine the materiality level or levels to be applied to particular classes of transactions, account balances or disclosures if, in the specific circumstances of the entity, there is one or more particular classes of transactions, account balances or disclosures for which misstatements of lesser amounts than materiality for the financial statements as a whole could reasonably be expected to influence the economic decisions of users taken on the basis of the financial statements.⁴⁵ However, this ISA does not require a different component performance materiality to be established for each class of transaction, account balance or disclosure for a component.

A72. Factors the group engagement may take into account in setting component performance materiality include the following:

- The extent of disaggregation of the financial information across components (e.g., as the extent of disaggregation across components increases, a lower component performance materiality generally would be appropriate to address aggregation risk). The relative significance of the component to the group may affect the extent of disaggregation (e.g., if a single component represents a large portion of the group, there likely may be less disaggregation across components).
- Expectations about the nature, frequency, and magnitude of misstatements in the component financial information, for example:
 - Whether there are risks that are unique to the financial information of the component (e.g., industry-specific accounting matters, unusual or complex

⁴³ ISA 550, paragraph 2

⁴⁴ ISA 200, paragraphs A53–A54

⁴⁵ ISA 320, paragraph 10

transactions).

- The nature and extent of misstatements identified at the component in prior audits.

A73. In some cases, the group engagement team may perform further audit procedures on accounts, classes of transactions or disclosures that are aggregated. For example, audit procedures may be performed at the group level for an entire account or class of transactions as a single population. In such cases, group performance materiality often will be used for purposes of performing these procedures.

A74. The threshold for communicating uncorrected misstatements to the group engagement team is set at an amount equal to, or lower than, the amount regarded as clearly trivial for the group financial statements. In accordance with ISA 450,⁴⁶ this threshold is the amount below which misstatements would not need to be accumulated because the group engagement team expects that the accumulation of such amounts clearly would not have a material effect on the group financial statements.

Identifying and Assessing the Risks of Material Misstatement (Ref: Para. 28–29)

A75. The group engagement team's process to identify and assess the risks of material misstatement of the group financial statements is iterative and dynamic and may be more complex, particularly where the component's business activities are complex or specialized, or when there are many components across multiple locations. In applying ISA 315 (Revised 2019),⁴⁷ the group engagement team will develop initial expectations about the potential risks of material misstatement and an initial identification of the significant classes of transactions, account balances and disclosures of the group financial statements based on their understanding of the group and its environment, the applicable financial reporting framework and the group's system of internal control.

A76. For the identified risks of material misstatement at the assertion level, a separate assessment of inherent risk and control risk is required by ISA 315 (Revised 2019). The group engagement team assesses the inherent risk by assessing the likelihood and magnitude of identified risks of material misstatement, taking into account the inherent risk factors. After identifying the risks of material misstatement, including those communicated by component auditors, the group engagement team determines the significant classes of transactions, account balances and disclosures of the group financial statements.

A77. The group engagement team's process (or the process of component auditors to whom risk assessment procedures are assigned) of assessing the identified risks of material misstatement at the assertion level also includes the determination of significant risks. Significant risks of the group financial statements that are included in components may be where the component has, for example:

- Accounting estimates that have high estimation uncertainty or complex models.
- A complex data collection and processing procedure (e.g., at a shared service center).
- Changes in the entity or business unit's activities, for example, a merger or acquisitions.

A78. If the group engagement team plans to test the operating effectiveness of controls, the auditor

⁴⁶ ISA 450, paragraph A3

⁴⁷ ISA 315 (Revised 2019), paragraph 22

shall assess control risk⁴⁸ (i.e. if the nature, timing and extent of the work to be performed on the consolidation process or the financial information of the components is based on an expectation that controls are operating effectively). The initial expectation of the operating effectiveness of controls is based on the group engagement team's or component auditor's evaluation of the design, and the determination of implementation, of the identified controls, including common controls.

Fraud (Ref: Para. 28)

A79. The auditor is required to identify and assess the risks of material misstatement of the financial statements due to fraud, and to design and implement appropriate responses to the assessed risks.⁴⁹ Information used to identify the risks of material misstatement of the group financial statements due to fraud may include the following:

- Group management's assessment of the risks that the group financial statements may be materially misstated as a result of fraud.
- Group management's process for identifying and responding to the risks of fraud in the group, including any specific fraud risks identified by group management, or classes of transactions, account balances, or for which a risk of fraud is likely.
- Whether there are particular components for which the risks of material misstatement due to fraud is higher.
- Whether any fraud risk factors or indicators of management bias exist in the consolidation process.
- How those charged with governance of the group monitor group management's processes for identifying and responding to the risks of fraud in the group, and the controls group management has established to mitigate these risks.
- Responses of those charged with governance of the group, group management, appropriate individuals within the internal audit function (and if considered appropriate, component management, the component auditors, and others) to the group engagement team's inquiry whether they have knowledge of any actual, suspected, or alleged fraud affecting a component or the group.

Inherent Risk Factors (Ref: Para. 28)

A80. Appendix 3 sets out examples of characteristics of events and conditions that, individually or together, may indicate risks of material misstatement of the group financial statements, whether due to fraud or error.

Considerations When Component Auditors are Involved (Ref: Para. 29)

A81. The group engagement team may assign risk assessment procedures related to the identification and the assessment of the risks of material misstatement of the group financial statements that result from inherent risk factors related to the financial information of a component, including how inherent risk factors related to the financial information of the component may affect the susceptibility of assertions to misstatement in the preparation of the group financial statements. For example, the group engagement team may work with component auditors to develop initial expectations about potential risks of material

⁴⁸ ISA 315 (Revised 2019), paragraph 34

⁴⁹ ISA 240, *The Auditor's Responsibilities Relating to Fraud in an Audit of Financial Statements*

misstatement of the group financial statements, including significant risks, related to components. The group engagement team discusses these matters with component auditors in accordance with paragraph 23. Factors that influence the group engagement team's decision whether to involve component auditors are included in paragraph A68.

- A82. The identification and assessment of inherent risk and control risk may be performed in different ways depending on preferred audit techniques or methodologies and may be expressed in different ways. Accordingly, when risk assessment procedures have been assigned to component auditors, the group engagement team may need to discuss its preferred approach with component auditors, or provide instructions, particularly where the group engagement team does not share common audit techniques, methodologies or training with component auditors.
- A83. In accordance with ISA 315 (Revised 2019),⁵⁰ the auditor is required to evaluate whether the audit evidence obtained from the risk assessment procedures provides an appropriate basis for the identification and assessment of the risks of material misstatement. Accordingly, when risk assessment procedures related to the identification and assessment of the risks of material misstatement of the group financial statements are assigned to component auditors, the group engagement team considers the results of the component auditor's work and, in applying ISA 315 (Revised 2019), determines whether the component auditor's work together with the work of the group engagement team, provides an appropriate basis for the identification and assessment of the risks of material misstatement of the group financial statements.
- A84. Based on the risk assessment procedures performed, the group engagement team may determine that an assessed risk of material misstatement of the group financial statements only arises in relation to financial information of certain components. For example, the risk of material misstatement relating to a legal claim may only exist in entities or business units that operate in a certain jurisdiction..

Responding to the Assessed Risks of Material Misstatement (Ref: Para. 30)

- A85. In responding to the assessed risks of material misstatement of the group financial statements, different approaches are available to the group engagement team to obtain audit evidence on classes of transactions, account balances and disclosures across the various components. Paragraphs A86 to A94 provide guidance to assist the group engagement team in determining an appropriate approach, or combination of approaches, for the engagement team to obtain audit evidence. Paragraphs A97 to A102 provide guidance on the options available to the group engagement team for assigning further audit procedures to component auditors to obtain audit evidence on the financial information of components for the purpose of the group financial statements.

Scoping a Group Audit

- A86. The group engagement team may design and perform further audit procedures centrally if the audit evidence to be obtained from performing further audit procedures on one or more classes of transactions, account balances or disclosures in the aggregate will respond to the assessed risks of material misstatement. For example, if the accounting records for the revenue transactions of the entire group are maintained centrally for the group (e.g., at a shared service center), the group engagement team may perform, or request a component

⁵⁰ ISA 315 (Revised 2019), paragraph 35

auditor to perform, further audit procedures to address the assessed risks of material misstatement of the related classes of transactions, account balances, and disclosures.

- A87. As the complexity and the diversity of the group increases (e.g., if the group has many different revenue streams, multiple lines of business, operates across multiple locations or has de-centralized systems of internal control), the group engagement team may find it more difficult to perform further audit procedures centrally. In such circumstances, the risks of material misstatement at the group financial statement level that are related to the financial information of a component may be effectively performed at the component level.
- A88. The group engagement team may determine that the financial information of several components can be considered as one population for the purpose of performing further audit procedures, for example, when transactions are considered to be homogenous because they share the same characteristics, the related risks of material misstatement are the same, and controls are designed and operating in a consistent way).
- A89. The group engagement team may have identified a significant class of transactions, account balance or disclosure in the group financial statements that comprises classes of transactions, account balances or disclosures at many components, none of which individually result in a risk of material misstatement at the group financial statement level. To obtain sufficient appropriate audit evidence, audit procedures on these classes of transactions, account balances or disclosures may be performed centrally if they are homogeneous, subject to common controls and access to appropriate information can be obtained. If this is not the case, the engagement team may need to perform audit procedures at selected components.
- A90. The group engagement team may perform substantive analytical procedures in accordance with ISA 520⁵¹ to address the risks of material misstatement at the assertion level for classes of transactions, account balances or disclosures in the group financial statements. Depending on the circumstances of the engagement, the financial information of the components may be aggregated by the group engagement team at various levels for purposes of developing expectations and determining the amount of any difference of recorded amounts from expected values in performing the substantive analytical procedures.

Element of Unpredictability

- A91. Including an element of unpredictability in the type of work to be performed, the components at which procedures are performed and the extent to which the group engagement team is involved in the work, may increase the likelihood of identifying a material misstatement of the components' financial information that may give rise to a material misstatement due to fraud of the group financial statements.⁵²

Operating Effectiveness of Controls that Are Common Across the Group

- A92. If the group engagement team intends to rely on the operating effectiveness of controls that operate throughout the group in determining the nature, timing and extent of substantive procedures to be performed at either the group level or at the components, the group engagement team, in accordance with ISA 330, is required to design and perform tests of controls to obtain sufficient appropriate audit evidence as to the operating effectiveness of those controls. This includes obtaining sufficient appropriate audit evidence that the controls

⁵¹ ISA 520, *Analytical Procedures*

⁵² ISA 240, paragraph 30(c)

are operating at the components as designed. The group engagement team may request the component auditor to assist the group engagement team in performing these procedures.

A93. If more deviations than expected are detected, the group engagement team may need to revise the audit plan. Possible revisions to the audit plan may include:

- Requesting additional substantive procedures to be performed at certain components.
- Increasing in the number of components selected for further audit procedures.
- Identifying and testing the operating effectiveness of other relevant controls that are designed and implemented effectively.

A94. Audit evidence obtained in determining whether common controls have been implemented and testing their operating effectiveness at selected components (including when component auditors perform such testing), may corroborate or contradict the conclusion that such controls have been implemented and are operating effectively commonly across a group.

Consolidation Process

Consolidation Procedures (Ref: Para. 31(a))

A95. The further audit procedures on the consolidation, including sub-consolidations, may include:

- Determining that all journal entries necessary are reflected in the consolidation; and
- Evaluating the operating effectiveness of the controls over the consolidation process and responding appropriately if any controls are determined to be ineffective.

Consolidation Adjustments and Reclassifications (Ref: Para. 31(b))

A96. The consolidation process may require adjustments and reclassifications to amounts reported in the group financial statements that do not pass through the usual IT applications, and may not be subject to the same controls to which other financial information is subject. The group engagement team's evaluation of the appropriateness, completeness and accuracy of the adjustments and reclassifications may include:

- Evaluating whether significant adjustments appropriately reflect the events and transactions underlying them;
- Determining whether those entities or business units whose financial information has been included in the group financial statements were appropriately included and valued in the consolidation process as required by the financial reporting framework;
- Determining whether significant adjustments have been correctly calculated, processed and authorized by group management and, where applicable, by component management;
- Determining whether significant adjustments are properly supported and sufficiently documented; and
- Checking the reconciliation and elimination of intra-group transactions and unrealized profits, and intra-group account balances.

Considerations when Component Auditors Are Involved (Ref: Para. 33)

A97. Component auditors may have a more in-depth knowledge of the components than the group engagement team, and therefore the group engagement team may need the assistance of the component auditor to determine the nature, timing and extent of further audit procedures

to be performed on the financial information of the component auditor.

A98. Circumstances in which the group engagement team may determine it is more effective to request that the component auditor design and perform further audit procedures related to a component may include situations in which there is a risk of material misstatement of the group financial statements due to the existence of events or conditions at the component:

- That may be relevant to group management's assessment of the group's ability to continue as a going concern; or
- That may affect the group auditor's response to risks of material misstatement relating to the valuation of the assets and liabilities of a component included in the group financial statements (i.e., circumstances in which the going concern basis of accounting may no longer be appropriate for the assets and liabilities of the component).

A99. In assigning further audit procedures to component auditors, the group engagement team may request component auditors to perform one or more of the following:

- Design and perform further audit procedures on the entire financial information of the component;
- Design and perform further audit procedures on one or more classes of transactions, account balances or disclosures; or
- Perform specific further audit procedures as identified and communicated by the group engagement team.

A100. The group engagement team may determine that audit evidence needs to be obtained on all or a significant proportion of a component's financial information to respond to the assessed risks of material misstatement of the group financial statements. In such circumstances, the group engagement team may determine that it is more effective to request that the component auditor design and perform further audit procedures on the entire financial information of the component. In such circumstances, the component auditor may need to evaluate whether sufficient appropriate audit evidence has been obtained with respect to the financial information of the component.

A101. The group engagement team may determine that audit evidence needs to be obtained on one or more classes of transactions, account balances, or disclosures of the financial information of a component. In such circumstances, the group engagement team may request that the component auditor performs further audit procedures on the classes of transactions, account balances or disclosures and may assign the design and performance of further audit procedures to the component auditor. The component auditor may also evaluate whether sufficient, appropriate audit evidence has been obtained.

A102. The group engagement team may request a component auditor to perform specific further audit procedures on the financial information of a component to respond to the assessed risks of material misstatement of the group financial statements. In such circumstances, the group engagement team determines the overall nature, timing and extent of procedures to be performed and appropriateness of those procedures for obtaining the audit evidence needed to respond to the assessed risks of material misstatement of the group financial statements.

Consolidation Process(Ref: Para. 36)

A103. The appropriate level of the group engagement team's involvement may depend on the circumstances and the structure of the group and other factors, such as the group engagement team's previous experience with the component auditors that perform procedures on the consolidation and sub-consolidations (also see paragraph A47) and the circumstances of the group audit engagement (e.g., if the financial information of an entity or business unit has not been prepared in accordance with the same accounting policies applied to the group financial statements).

Using Audit Evidence from an Audit Performed for Another Purpose (Ref: Para. 39)

A104. In limited circumstances, an audit may be performed on the financial statements of an entity or business unit that is part of the group, and an auditor's report has been issued for statutory, regulatory or other reasons. This may be the case, for example, when an entity or business unit has been acquired close to year-end. If an audit has been performed and an auditor's report has been issued for statutory, regulatory or other reasons, the group engagement team may use audit evidence from that audit if the group engagement team is satisfied that the work is appropriate for the group engagement team's purposes. If the audit procedures performed are not an appropriate response to the assessed risks of material misstatement of the group financial statements, the group engagement team may decide not to use the audit evidence from that audit. Alternatively, the group engagement team may plan to have additional audit procedures performed on the component, to address the assessed risks of material misstatement of the group financial statements.

A105. Factors that may affect the group engagement team's decision whether to use the audit evidence from an audit that has already been performed due to statutory, regulatory or other reasons to provide audit evidence for the group audit may include the following:

- Differences in the financial reporting framework applied in preparing the financial statements of the entity or business unit and that applied in preparing the group financial statements.
- Differences in the auditing and other standards applied by the component auditor and those applied in the audit of the group financial statements.
- Differences in the financial reporting period-end between the financial statements of the entity or business unit and the financial statements of the group.

A106. Other relevant requirements in this ISA with respect to the use of the work of a component auditor as described in paragraph 39(c), may include the requirements in the sections on understanding the group and its environment, the applicable financial reporting framework and the group's system of internal control, materiality, identifying and assessing the risks of material misstatement, responding to the assessed risks of material misstatement and two-way communication between the group engagement team and the component auditor.

Two-Way Communication Between the Group Engagement Team and the Component Auditor

Effective Two-Way Communication (Ref: Para. 40)

A107. Clear communication of the group engagement team's and the component auditor's responsibilities, the timing of the group audit and the expected general content of the communications helps establish the basis for effective two-way communication. If effective two-way communication between the group engagement team and the component auditors

does not exist, there is a risk that the group engagement team may not obtain sufficient appropriate audit evidence on which to base the group audit opinion.

A108. Factors that may also contribute to effective two-way communication include:

- A mutual understanding of relevant issues and the expected actions arising from the communication process.
- The manner in which communications will be made. For example, it may be better to discuss certain matters in person than by exchanging emails.
- The person(s) in the group engagement team who will communicate regarding particular matters.
- The group engagement team's expectations that communication will be two-way, and that the component auditor is expected to communicate timely with the group engagement team matters they consider relevant to the group audit.
- The process for taking action and reporting back on matters communicated by the group engagement team.

Form of Communication (Ref: Para. 40)

A109. The group engagement team's requirements are often communicated in a letter of instruction. The component auditor's communication with the group engagement team often takes the form of a memorandum or report of work performed. Communication between the group engagement team and the component auditor, however, may not necessarily be in writing. For example, the group engagement team may visit the component auditor to discuss identified significant risks or review relevant parts of the component auditor's audit documentation. Nevertheless, the documentation requirements of this and other ISAs apply.

A110. The form of communication may be affected by such factors as:

- The significance, complexity or urgency of the matter.
- Whether the matter will be communicated to group management and those charged with governance of the group.

Timing of Communications (Ref: Para. 40)

A111. The appropriate timing for communications will vary with the circumstances of the engagement. Relevant circumstances may include the nature, timing and extent of work to be performed by the component auditor and the action expected to be taken by the component auditor. For example, communications regarding planning matters may often be made early in the audit engagement and, for an initial engagement, may be made as part of agreeing the terms of the engagement.

Non-Compliance with Laws or Regulations (Ref: Para. 18, 40)

A112. The group engagement partner may become aware of information about non-compliance or suspected non-compliance with laws or regulations. In such circumstances, the group engagement partner may have an obligation under relevant ethical requirements, laws or regulations, to communicate the matter to the component auditor.⁵³

⁵³ See, for example, Section 360.17 and Section 360.18 of the International Ethics Standards Board for Accountants' *Code of Ethics for Professional Accountants*

Reviewing the Component Auditor's Audit Documentation (Ref: Para. 42(b))

A113. The audit documentation of the component auditor that will be relevant to the group audit may vary depending on the circumstances. The nature, timing and extent of the review may be affected by:

- (a) The identified risks of material misstatement of the group financial statements, including the degree to which the component auditor was involved in risk assessment procedures and in the identification and assessment of those risks;
- (b) The group engagement team's understanding of the component auditor, including the competence and capabilities of the component auditor; and
- (c) The fact that the component auditor's audit documentation has been subjected to the component auditor's firm's review procedures.

Subsequent Events (Ref: Para. 44)

A114. The group engagement team may:

- (a) Request a component auditor to perform subsequent events procedures to assist the group engagement team to identify events that occur between the dates of the financial information of the components and the date of the auditor's report on the group financial statements.
- (b) Perform procedures to cover the period between the date of communication of subsequent events by the component auditor and the date of the auditor's report on the group financial statements.

Evaluating the Sufficiency and Appropriateness of Audit Evidence Obtained

Sufficiency and Appropriateness of Audit Evidence (Ref: Para. 45)

A115. The evaluation required by paragraph 45 assists the group engagement team in determining whether the overall group audit strategy and group audit plan developed to respond to the assessed risks of material misstatement of the group financial statements continues to be appropriate. The requirement in ISA 330⁵⁴ for the auditor, irrespective of the assessed risks of material misstatement, to design and perform substantive procedures for each material account balance, class of transactions and disclosure also may be helpful for purposes of this evaluation in the context of the group financial statements.

A116. If the group engagement team concludes that sufficient appropriate audit evidence on which to base the group audit opinion has not been obtained, the group engagement team may request the component auditor to perform additional procedures or may perform its own procedures in relation to the component.

Evaluating the Effect on the Group Audit Opinion (Ref: Para. 46)

A117. The group engagement partner's evaluation also may include a consideration of whether misstatements communicated by component auditors indicate a systemic issue (e.g., with respect to transactions subject to common accounting policies or common controls) that may affect other components.

⁵⁴ ISA 330, paragraph 18

Auditor's Report (Ref: Para. 48)

A118. Although component auditors may perform work on the financial information of the components for the group audit and as such are responsible for their overall findings, conclusions or opinions, the group engagement partner or the group engagement partner's firm is responsible for the group audit opinion.

A119. When the group audit opinion is modified because the group engagement team was unable to obtain sufficient appropriate audit evidence in relation to the financial information of one or more components, the Basis for Qualified Opinion or Basis for Disclaimer of Opinion section in the auditor's report on the group financial statements describes the reasons for that inability without referring to the component auditor, unless such a reference is necessary for an adequate explanation of the circumstances.⁵⁵

Communication with Group Management and Those Charged with Governance of the Group

Engagement Partner's Review (Ref: Para. 49)

A120. The group engagement partner is not expected to review, prior to their issuance, all communications between a component auditor and component management unless the communications are of significance to the audit of the group financial statements. The group engagement partner may inform component auditors of their responsibilities in identifying communications that may be significant to the group audit engagement.

Communication with Group Management (Ref: Para. 50–51)

A121. ISA 240 contains requirements and guidance on communication of fraud to management and, where management may be involved in the fraud, to those charged with governance.⁵⁶

A122. Group management may need to keep certain material sensitive information confidential. Examples of matters that may be significant to the financial statements of the component of which component management may be unaware include the following:

- Potential litigation.
- Plans for abandonment of material operating assets.
- Subsequent events.
- Significant legal agreements.

Communication with Those Charged with Governance of the Group (Ref: Para. 52)

A123. The matters the group engagement team communicates to those charged with governance of the group may include those brought to the attention of the group engagement team by component auditors that the group engagement team judges to be significant to the responsibilities of those charged with governance of the group. Communication with those charged with governance of the group takes place at various times during the group audit. For example, the matter referred to in paragraph 52(a) may be communicated after the group engagement team has determined the work to be performed on the financial information of the components. On the other hand, the matter referred to in paragraph 52(b) may be communicated at the end of the audit, and the matters referred to in paragraph 52(c)–(d) may

⁵⁵ ISA 705 (Revised), paragraphs 20 and 24

⁵⁶ ISA 240, paragraphs 41–43

be communicated when they occur.

Documentation (Ref: Para. 53)

A124. In accordance with ISA 230,⁵⁷ the audit documentation for a group audit engagement needs to be sufficient to enable an experienced auditor, having no previous connection with the audit, to understand the audit procedures performed, the evidence obtained, and the conclusions reached with respect to significant matters arising during the group audit. The audit documentation for the group audit includes documentation of the nature, timing and extent of the work performed by component auditors related to a component (component auditor documentation). Such documentation may reside in the component auditor's audit file and need not be replicated in the group engagement team's audit file. The extent to which component auditor documentation is included in the group engagement team's audit file is a matter of professional judgment.

Documentation of the Direction and Supervision of Component Auditors and the Review of Their Work (Ref: Para. 53(c))

A125. ISA 300⁵⁸ requires the auditor to describe, in the audit plan, the nature, timing and extent of the planned direction and supervision of engagement team members and the review of their work.

A126. When component auditors are involved in the group audit, the group engagement team's documentation of its involvement in the work of component auditors may include, for example:

- Required communications with component auditors, including instructions issued and other confirmations required by this ISA.
- The rationale for the selection of visits to component auditor sites, attendees at meetings and the nature of the matters discussed.
- Matters discussed in teleconferences or videoconferences with component auditors or component management.
- The rationale for the group engagement team's determination of audit documentation selected for review.
- Changes in the planned nature and extent of involvement with component auditors, and the reasons why.

A127. The determination of the nature and extent of the review of component auditor documentation by the group engagement team is also a matter of professional judgment. Paragraph A113 includes factors that may affect the determination of the extent of the review of audit documentation of component auditors.

A128. Policies or procedures established by the firm in accordance with the firm's system of quality management, or resources provided by the firm or a network, may assist the group engagement team in documenting the direction and supervision of component auditors and the review of their work. For example, the firm may have developed an electronic audit tool that may be used to facilitate communications between the group engagement team and component auditors, and such tool also is used for audit documentation.

⁵⁷ ISA 230, paragraphs 8 and 9

⁵⁸ ISA 300, *Planning an Audit of Financial Statements*, paragraph 9(a).

Other Documentation Considerations When Access to Component Auditor Documentation is Restricted (Ref: Para. 53)

A129. Audit documentation for an audit of group financial statements may present some additional complexities or challenges depending the structure of the group. This may be the case, for example, when the group has entities or business units in a number of different jurisdictions with varying laws or regulations that may limit the ability of the group engagement team to include relevant parts of the component auditor documentation in the group engagement team's audit file.

A130. When access to component auditors or component auditor documentation is restricted, the group engagement team is nonetheless required to obtain sufficient appropriate audit evidence to provide a basis for forming an opinion on the group financial statements. In addition, when relevant parts of the component auditor documentation are unable to be included in the group engagement team's audit file, the group engagement team may need to prepare documentation that reflects the procedures performed, evidence obtained and conclusions reached by the component auditor on matters relevant to the group financial statements. The group engagement team uses professional judgment in determining the nature and extent of such documentation to include in the group engagement team's audit file, in view of the requirements of ISA 230.

Appendix 1
(Ref: Para. A29)

Illustration of Independent Auditor’s Report Where the Group Engagement Team Is Not Able to Obtain Sufficient Appropriate Audit Evidence on Which to Base the Group Audit Opinion

For purposes of this illustrative auditor’s report, the following circumstances are assumed:

- **Audit of a complete set of consolidated financial statements of an entity other than a listed entity using a fair presentation framework. The audit is a group audit (i.e., ISA 600 (Revised) applies).**
- **The consolidated financial statements are prepared by management of the entity in accordance with IFRSs (a general purpose framework).**
- **The terms of the audit engagement reflect the description of management’s responsibility for the consolidated financial statements in ISA 210.**
- **The group engagement team is unable to obtain sufficient appropriate audit evidence relating to a component accounted for by the equity method (recognized at \$15 million in the statement of financial position, which reflects total assets of \$60 million) because the group engagement team did not have access to the accounting records, management, or auditor of the component.**
- **The group engagement team has read the audited financial statements of the component as at December 31, 20X1, including the auditor’s report thereon, and considered related financial information kept by group management in relation to the component.**
- **In the group engagement partner’s judgment, the effect on the group financial statements of this inability to obtain sufficient appropriate audit evidence is material but not pervasive.⁵⁹**
- **The International Ethics Standards Board for Accountants’ Code of Ethics for Professional Accountants comprises all of the relevant ethical requirements that apply to the audit.**
- **Based on the audit evidence obtained, the auditor has concluded that a material uncertainty does not exist related to events or conditions that may cast significant doubt on the entity’s ability to continue as a going concern in accordance with ISA 570 (Revised).**
- **The auditor is not required, and has otherwise not decided, to communicate key audit matters in accordance with ISA 701.⁶⁰**
- **The auditor has obtained all of the other information prior to the date of the auditor’s report and the qualified opinion on the consolidated financial statements also affects the other information.**
- **Those responsible for oversight of the consolidated financial statements differ from**

⁵⁹ If, in the group engagement partner’s judgment, the effect on the group financial statements of the inability to obtain sufficient appropriate audit evidence is material and pervasive, the group engagement partner would disclaim an opinion in accordance with ISA 705 (Revised).

⁶⁰ ISA 701, *Communicating Key Audit Matters in the Independent Auditor’s Report*

- **those responsible for the preparation of the consolidated financial statements.**
- **In addition to the audit of the consolidated financial statements, the auditor has other reporting responsibilities required under local law.**

INDEPENDENT AUDITOR’S REPORT

To the Shareholders of ABC Company [or Other Appropriate Addressee]

Report on the Audit of the Consolidated Financial Statements⁶¹

Qualified Opinion

We have audited the consolidated financial statements of ABC Company and its subsidiaries (the Group), which comprise the consolidated statement of financial position as at December 31, 20X1, and the consolidated statement of comprehensive income, consolidated statement of changes in equity and consolidated statement of cash flows for the year then ended, and notes to the consolidated financial statements, including a summary of significant accounting policies.

In our opinion, except for the possible effects of the matter described in the Basis for Qualified Opinion section of our report, the accompanying consolidated financial statements present fairly, in all material respects (or give a true and fair view of), the consolidated financial position of the Group as at December 31, 20X1, and (of) their consolidated financial performance and consolidated cash flows for the year then ended in accordance with International Financial Reporting Standards (IFRSs).

Basis for Qualified Opinion

ABC Company’s investment in XYZ Company, a foreign associate acquired during the year and accounted for by the equity method, is carried at \$15 million on the consolidated statement of financial position as at December 31, 20X1, and ABC’s share of XYZ’s net income of \$1 million is included in the consolidated statement of comprehensive income for the year then ended. We were unable to obtain sufficient appropriate audit evidence about the carrying amount of ABC’s investment in XYZ as at December 31, 20X1 and ABC’s share of XYZ’s net income for the year because we were denied access to the financial information, management, and the auditors of XYZ. Consequently, we were unable to determine whether any adjustments to these amounts were necessary.

We conducted our audit in accordance with International Standards on Auditing (ISAs). Our responsibilities under those standards are further described in the *Auditor’s Responsibilities for the Audit of the Consolidated Financial Statements* section of our report. We are independent of the Group in accordance with the International Ethics Standards Board for Accountants’ *Code of Ethics for Professional Accountants* (IESBA Code), and we have fulfilled our other ethical responsibilities in accordance with the IESBA Code. We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our qualified audit opinion.

Other Information [or another title if appropriate such as “Information Other than the Financial Statements and Auditor’s Report Thereon”]

[Reporting in accordance with the reporting requirements in ISA 720 (Revised)⁶² – see Illustration

⁶¹ The sub-title, “Report on the Audit of the Consolidated Financial Statements” is unnecessary in circumstances when the second sub-title, “Report on Other Legal and Regulatory Requirements” is not applicable.

⁶² ISA 720 (Revised), *The Auditor’s Responsibilities Relating to Other Information*

6 in Appendix 2 of ISA 720 (Revised). The last paragraph of the other information section in Illustration 6 would be customized to describe the specific matter giving rise to the qualified opinion that also affects the other information.]

Responsibilities of Management and Those Charged with Governance for the Consolidated Financial Statements⁶³

[Reporting in accordance with ISA 700 (Revised)⁶⁴ – see Illustration 2 in ISA 700 (Revised).]

Auditor’s Responsibilities for the Audit of the Consolidated Financial Statements

[Reporting in accordance with ISA 700 (Revised) – see Illustration 2 in ISA 700 (Revised). The last two paragraphs which are applicable for audits of listed entities only would not be included.]

Report on Other Legal and Regulatory Requirements

[Reporting in accordance with ISA 700 (Revised) – see Illustration 2 in ISA 700 (Revised).]

[Signature in the name of the audit firm, the personal name of the auditor, or both, as appropriate for the particular jurisdiction]

[Auditor Address]

[Date]

If, in the group engagement partner’s judgment, the effect on the group financial statements of the inability to obtain sufficient appropriate audit evidence is material and pervasive, the group engagement partner would disclaim an opinion in accordance with ISA 705 (Revised).

⁶³ Throughout these illustrative auditor’s reports, the terms management and those charged with governance may need to be replaced by another term that is appropriate in the context of the legal framework in the particular jurisdiction.

⁶⁴ ISA 700 (Revised), *Forming an Opinion and Reporting on Financial Statements*

Appendix 2

(Ref: Para. A49)

Understanding the Group's System of Internal Control

1. This appendix provides examples of controls that may be helpful in obtaining an understanding of the system of internal control in a group environment, and expands on how ISA 315 (Revised 2019) is to be applied in relation to an audit of group financial statements.⁶⁵ The examples may not be relevant to every group audit engagement and the list of examples is not necessarily complete.

Control Environment

2. The group engagement team's understanding of the control environment may include matters such as the following:
 - The structure of the governance and management functions across the group, and group management's oversight responsibilities, including arrangements for assigning authority and responsibility to management of entities or business units in the group.
 - How oversight over the group's system of internal control by, those charged with governance is structured and organized.
 - How ethical and behavioral standards are communicated and reinforced in practice across the group, (e.g., group-wide programs, such as codes of conduct and fraud prevention programs).
 - The consistency of policies and procedures across the group, including a group financial reporting procedures manual.

The Group's Risk Assessment Process

3. The group engagement team's understanding of the group's risk assessment process may include matters such as group management's risk assessment process, that is, the process for identifying, analyzing and managing business risks, including the risk of fraud, that may result in material misstatement of the group financial statements.

The Group's Process to Monitor the System of Internal Control

4. The group engagement team's understanding of the group's process to monitor the system of internal control may include matters such as monitoring of controls, including how the controls are monitored across the group and, where relevant, activities of the internal audit function across the group. The group's internal audit function, including its nature, responsibilities and activities in respect of monitoring of controls at entities or business units in the group. ISA 610 (Revised 2013)⁶⁶ deals with the group engagement team's evaluation of whether the internal audit function's organizational status and relevant policies and procedures adequately supports the objectivity of internal auditors, the level of competence of the internal audit function, and whether the function applies a systematic and disciplined approach where the group audit team expects to use the function's work.

⁶⁵ ISA 315 (Revised 2019), Appendix 3

⁶⁶ ISA 610 (Revised 2013), *Using the Work of Internal Auditors*, paragraph 15

The Information System and Communication

5. The group engagement team's understanding of the group's information system and communication may include matters such as the following:
- Group management's monitoring of operations and the financial results of entities or business units in the group, including regular reporting routines, which enables group management to monitor performance against budgets, and to take appropriate action.
 - Monitoring, controlling, reconciling, and eliminating intra-group transactions and unrealized profits, and intra-group account balances at group level.
 - A process for monitoring the timeliness and assessing the accuracy and completeness of financial information received from entities or business units in the group.

Consolidation Process

6. The group engagement team's understanding of the consolidation process may include matters such as the following:

Matters relating to the applicable financial reporting framework:

- The extent to which management of entities or business units in the group have an understanding of the applicable financial reporting framework.
- The process for identifying and accounting for entities or business units in the group in accordance with the applicable financial reporting framework.
- The process for identifying reportable segments for segment reporting in accordance with the applicable financial reporting framework.
- The process for identifying related party relationships and related party transactions for reporting in accordance with the applicable financial reporting framework.
- The accounting policies applied to the group financial statements, changes from those of the previous financial year, and changes resulting from new or revised standards under the applicable financial reporting framework.
- The procedures for dealing with entities or business units in the group with financial year-ends different from the group's year-end.

Matters relating to the consolidation process:

- Group management's process for obtaining an understanding of the accounting policies used by entities or business units in the group, and, where applicable, ensuring that uniform accounting policies are used to prepare the financial information of the entities or business units in the group for the group financial statements, and that differences in accounting policies are identified, and adjusted where required in terms of the applicable financial reporting framework. Uniform accounting policies are the specific principles, bases, conventions, rules, and practices adopted by the group, based on the applicable financial reporting framework, that the entities or business units in the group use to report similar transactions consistently. These policies are ordinarily described in the financial reporting procedures manual and reporting package issued by group management.
- Group management's process for ensuring complete, accurate and timely financial reporting

by the entities or business units in the group for the consolidation.

- The process for translating the financial information of foreign entities or business units in the group into the currency of the group financial statements.
- How the group's IT environment is organized for the consolidation and the policies that define the flows of information in the consolidation process, including the IT applications involved.
- Group management's process for obtaining information on subsequent events.

Matters relating to consolidation adjustments and reclassifications:

- The process for recording consolidation adjustments, including the preparation, authorization and processing of related journal entries, and the experience of personnel responsible for the consolidation.
- The consolidation adjustments required by the applicable financial reporting framework.
- The business rationale for the events and transactions that gave rise to the consolidation adjustments.
- Frequency, nature and size of transactions between entities or business units in the group.
- The procedures for monitoring, controlling, reconciling and eliminating intra-group transactions and unrealized profits, and intra-group account balances.
- Steps taken to arrive at the fair value of acquired assets and liabilities, procedures for amortizing goodwill (where applicable), and impairment testing of goodwill, in accordance with the applicable financial reporting framework.
- Arrangements with a majority owner or minority interests regarding losses incurred by an entity or business unit in the group (e.g., an obligation of the minority interest to make good such losses).

Control Activities

7. The group engagement team's understanding of the control activities component may include matters such as the following:
 - The extent of centralization in the group's IT environment and the commonality of IT applications, IT processes and IT infrastructure.
 - The commonality of information processing controls and general IT controls for all or part of the group.
 - The extent of the commonality of the design of controls for all or part of the group that address risks of material misstatement of the group financial statements at the assertion level.
 - The extent to which commonly designed controls have been implemented consistently for all or part of the group.

Appendix 3

(Ref: Para. A80)

Examples of Events or Conditions that May Give Rise to Risks of Material Misstatement of the Group Financial Statements

The following are examples of events (including transactions) and conditions that may indicate the existence of risks of material misstatement in the group financial statements, at the financial statement level or the assertion level. The examples provided by inherent risk factor cover a broad range of events and conditions; however, not all events and conditions are relevant to every group audit engagement and the list of examples is not necessarily complete. The events and conditions have been categorized by the inherent risk factor that may have the greatest effect in the circumstances. Importantly, due to the interrelationships among inherent risk factors, the example events and conditions also are likely to be subject to, or affected by, other inherent risk factors to varying degree. Also see ISA 315 (Revised 2019), Appendix 2.

Inherent Risk Factor	Examples of Events or Conditions that May Give Rise to the Existence of Risks of Material Misstatement of the Group Financial Statements at the Assertion Level:
Complexity	<ul style="list-style-type: none"> • The existence of complex transactions that are accounted for in more than one entity or business units in the group. • The application of accounting policies by entities or business units in the group that differ from those applied to the group financial statements. • Accounting measurements or disclosures that involve complex processes used by entities or business units in the group such as accounting for complex financial instruments. • Operations that are subject to a high degree of complex regulation in multiple jurisdictions, or entities or business units in the group that operate in multiple industries that are subject to different types of regulation.
Subjectivity	<ul style="list-style-type: none"> • Judgments regarding which entities or business units in the group require incorporation of their financial information in the group financial statements in accordance with the applicable financial reporting framework, for example, whether any special-purpose entities or non-trading entities exist and require incorporation. • Judgments regarding the correct application of the requirements of the applicable financial reporting framework by entities or business units in the group.
Change	<ul style="list-style-type: none"> • Frequent acquisitions, disposals or reorganizations.
Uncertainty	<ul style="list-style-type: none"> • Entities or business units in the group operating in foreign jurisdictions that may be exposed to factors such as unusual government intervention in areas such as trade and fiscal policy, and restrictions on currency and dividend movements; and

	fluctuations in exchange rates.
Susceptibility to Misstatement Due to Management Bias or Other Fraud Risk Factors Insofar as They Affect Inherent Risk	<ul style="list-style-type: none"> • Unusual related party relationships and transactions. • Entities or business units in the group with different financial year-ends, which may be utilized to manipulate the timing of transactions. • Prior occurrences of unauthorized or incomplete consolidation adjustments. • Aggressive tax planning within the group, or large cash transactions with entities in tax havens. • Prior occurrences of intra-group account balances that did not balance or reconcile on consolidation.

Indicators that the control environment, the group's risk assessment process or the group's process to monitor the group's system of internal control are not appropriate to the group's circumstances, considering the nature and complexity of the group, and do not provide an appropriate foundation for the other components of the group's system of internal control, include:

- Poor corporate governance structures, including decision-making processes that are not transparent.
- Non-existent or ineffective controls over the group's financial reporting process, including inadequate group management information on monitoring of operations and financial results of entities or business units in the group.



AUASB Board Meeting Summary Paper

AGENDA ITEM NO. 3.0
Meeting Date: 10 March 2020
Subject: ISQM 1
Date Prepared: 2 March 2020
Prepared by: Rene Herman

Action Required

For Information Purposes Only

A. Background

- 1 The IAASB issued ED-ISQM 1 in February 2019, with a comment period ending 1 July 2019.
- 2 The AUASB did extensive outreach on this Exposure Draft and [submitted a response to the IAASB](#).
- 3 A summary of the key points coming out of the AUASB's submission to the IAASB Exposure Draft includes:
 - (a) Size, structure and complexity – refer section C, paragraph 9 below.
 - (b) Level of granularity around the Risk Assessment Process (RAP), particularly in the approach to quality objectives and responses in the components – refer section C, paragraph 10 below.
 - (c) Threshold for assessing Quality Risks linked to remote – refer section C, paragraph 10 below.
 - (d) Monitoring and remediation – refer section C, paragraph 11 below.
 - (e) Use of technology and clarification sought on the scope of IT – refer section C, paragraph 12 below.
 - (f) Service Providers – refer section C, paragraph 13 below.
 - (g) Information and communication including communication with external parties – refer section C, paragraph 14 below.
 - (h) Evaluating the System of Quality Management – refer section C, paragraph 15 below.
 - (i) General scalability of the standard – refer section C, paragraph 16 below.
 - (j) Documentation – refer section C, paragraph 17 below.
- 4 The ISQM 1 taskforce have addressed many of the matters referred to above, see section C of this paper. The main area that the taskforce will still be doing additional outreach on is in the area of Networks – this will be shared with the IAASB at the March 2020 IAASB meeting in New York.

This document contains preliminary views and/or AUASB Technical Group recommendations to be considered at a meeting of the AUASB, and does not necessarily reflect the final decisions of the AUASB. No responsibility is taken for the results of actions or omissions to act on the basis of reliance on any information contained in this document (including any attachments), or for any errors or omissions in it.

B. What the Audit Technical Group (ATG) is seeking from the AUASB at the March 2020 AUASB meeting

5 The purpose of this Agenda Item is to update the AUASB as to the taskforces proposed way forward on issues raised by stakeholders (including AUASB).

6 In section C.9 – C.17 the ATG has highlighted the AUASBs and other respondents' key concerns and the taskforces current thinking. Additionally, section D of this paper, raises a few other matters for the AUASB's consideration. Where considered appropriate, the ATG has raised queries throughout this paper for the AUASB's consideration and input.

7 **The IAASB is aiming to vote out a final ISQM 1 at the June 2020 IAASB meeting. Accordingly, and in line with the AUASB International Strategy, AUASB members are encouraged to comment on any of these areas to inform the AUASB Chair of their views. AUASB members are reminded that this standard is drawing close to finalisation and that now is the best time to still influence areas of the standard.**

8 Since this summary paper references paragraphs of this document a link to the clean proposed ISQM 1 is provided [[here](#)]. Additionally, a clean copy of proposed ISQM 1 is included at Agenda Item 3.1.

C. Summary of ISQM 1 taskforce actions addressing the matters referred to in Section A of this paper:

9 *Size, structure and complexity of Standard*

Overall comments from the AUASB in the submission on ED-ISQM 1 highlighted concerns with complexity, prescriptiveness, repetitiveness of information and general length of the standard. This feedback was consistent with feedback received generally from respondents to ED-ISQM 1.

(a) To aid with the complexity, structure and length of the standard, ISQM- 1 has been restructured so that:

(i) The Risk Assessment Process is now near the front of the requirements, before the governance and leadership component. This has also facilitated a reduction in the introduction section.

(ii) The system of quality management at the beginning of the requirements section, has a link into governance and leadership to emphasise the importance of this component and that governance and leadership is a pre-requisite to setting up a SOQM.

(b) Drafting and presentation

(i) Example boxes have been used, with specific signposting to scalable examples.

(ii) Duplicate information removed e.g.: explanations in the introduction, appendix, repetitive AM.

(iii) Removal of AM that may only be relevant for a first time through – sperate guide to be introduced.

10 *Level of granularity around the Risk Assessment Process (RAP), particularly in the approach to quality objectives and responses in the components.*

Overall comments from the AUASB in the submission on ED-ISQM 1 highlighted concerns with the level of granularity around the Risk Assessment Process (RAP), particularly in the granular and

prescriptive approach to quality objectives and responses in the components. Additionally, the AUASB raised concerns regarding the requirement to always establish additional quality objectives over and above the objectives in the standard. Furthermore, the AUASB raised concerns that the pre-determined required responses may not be applicable where a firm has no associated risk. In relation to the Risk Assessment Process, the AUASB is directed to the requirements in paragraphs 22C-22G of the [updated proposed ISQM 1](#).

To address stakeholders' concerns (including those of the AUASB), the following changes have been made to ISQM 1:

- (a) Refining quality objectives by component to be outcome based incorporating some previous responses to quality objectives.
- (b) Introduced factors (conditions, events, circumstances that may adversely affect the achievement of the firm's quality objectives) as part of identifying and assessing quality risks, the firm understands the factors relating to:
 - o Nature and circumstances of the firm; and
 - o Nature and circumstances of the engagements performed by the firm.

The standards recognise that not all factors will give rise to quality risks.

- (c) Reduction in prescribed responses to quality risks – essentially up to the firm to determine their responses to achieve their quality objectives. Responses that have not been combined with an objective have been moved to separate section 'specified responses. The specified responses include responses to address: independence, acceptance and continuance and a placeholder for EQCR, all other responses have been included within the quality objective.
- (d) Amended the definition of quality risk to more directly refer to likelihood and magnitude:

Quality risks – Risks that have a reasonable possibility, individually or in combination with other quality risks, of:

 - (i) *Occurring (i.e., likelihood); and*
 - (ii) *Adversely affecting the achievement of a quality objective(s) if the risk were to occur (i.e., magnitude).*

<i>Question 1: Are AUASB members comfortable with the definition of Quality Risk?</i>
--

<i>Question 2: Are AUASB members comfortable with the way that Quality Objectives, Quality Risks and Responses have been addressed in the standard?</i>
--

- (e) Clarified that quality objectives beyond those set out in the standard may not always be required, however the objectives set out in the standard are all required. Additionally, clarified that quality risks and responses set out in the standard may be modified if the firm considers appropriate to modify.

11 *Monitoring and Remediation*

Overall comments from the AUASB in the submission on ED-ISQM 1 was consistent with other stakeholders' feedback. The comments raised by the AUASB were:

- o The requirement to inspect completed files was supported, but the AUASB considered that the requirement and application material could be more principles focused.

- The differences between findings and deficiencies was unclear with findings not being defined.
- Lack of clarity around when root-cause analysis is required and the lack of ‘flexing’ of such analysis.

In relation to Monitoring and Remediation, the AUASB is directed to the requirements in paragraphs 42-54 of the [updated proposed ISQM 1](#).

To address stakeholders’ concerns (including those of the AUASB), the following changes have been made to ISQM 1:

- (a) The definition of Deficiency¹ has been simplified and Findings has now been defined as:
Findings (in relation to a system of quality management) – Information about the design, implementation and operation of the system of quality management, which comprises:
 - (i) *The results of the firm’s monitoring activities and external inspections; and*
 - (ii) *Other information that indicates that one or more deficiencies may exist*
- (b) Application material A173-A177 has been included to provide clarity in determining whether a finding is a deficiency, noting that this requires the exercise of professional judgement. Application material A175 has been included to provide quantitative and qualitative factors that may be considered in making this determination.

Question 3: Are AUASB members comfortable with the definition of finding and is the distinction between finding and deficiency clear?

Question 4: Is it clear to AUASB members when root cause analysis is required?

- (c) The requirement in relation to selection of completed engagements for inspections has been supplemented with application material to emphasise that the selection is affected by the nature, timing and extent of tother monitoring activities undertaken by the firm – thereby providing improved flexibility for firms in determining the appropriate cycle for the inspection of completed engagements. Additionally, in order to improve the focus on the selection of engagements based on risks, there is additional application material paragraph A169A giving examples of how the firm may apply a cyclical basis for inspections – including flexing the period between selections up or down.

Question 5: Are AUASB members comfortable with the approach to addressing the inspection of completed files?

12 Use of Technology and clarification of scope of IT

Overall comments from the AUASB in the submission on ED-ISQM 1 supported how ED-ISQM 1 addressed technology, however there was a need to clarify the scope of technology contemplated by the standard. In relation to Technology (Resource), the AUASB is directed to the requirements in paragraph 38 of the [updated proposed ISQM 1](#).

To address stakeholders’ concerns (including those of the AUASB), the following changes have been made to ISQM 1:

- (a) Application material A125 has been amended to clarify the scope of technological resources that form part of the firm’s system of quality management, and to demonstrate how the

¹ Deficiency in the firm’s system of quality management (referred to as “deficiency” in this ISQM) – An aspect of the firm’s system of quality management is absent, inappropriately designed, or not operating effectively.

technological resources may vary depending on the nature and circumstances of the firm. The examples also aim to address scalability concerns of the technological resources' requirements.

13 *Service Providers*

Overall comments from the AUASB in the submission on ED-ISQM 1 supported the proposals addressing service providers in ISQM 1, but recommended that the term 'service provider' is more clearly defined within ISQM 1, with examples provided to assist practitioners identify not only who is a service provider captured under ISQM 1, but also to provide clarity as to who is outside the definition. In relation to Service Providers (Resource), the AUASB is directed to the requirements in paragraph 38 of the [updated proposed ISQM 1](#).

To address stakeholders' concerns (including those of the AUASB), the following changes have been made to ISQM 1:

- (a) Paragraph [h A134A explains what a service provider is, indicates who is not a service provider and provides examples of resources from a service provider.
- (b) One of the factors the firm considers when identifying an assessing quality risks is the resources of a firm including service providers (paragraph 22E(a)(i)(d). Service providers have been included under the resources component and is no longer a stand-alone section of the standard. The standard (A134B-A134C) recognises that the nature, timing and extent of the firm's responses to address service providers depends on the assessed quality risks identified by the firm i.e. not all resources from service providers will necessitate a response.

Question 6: Are AUASB members comfortable with the way in which service providers has been clarified?

14 *Information and Communication including communication with external parties*

The AUASB was supportive of guidance around appropriate communications with external parties, however the AUASB was concerned that transparency reports would be a requirement of the standard. In relation to Information and Communication, the AUASB is directed to the requirements in paragraph 40 of the [updated proposed ISQM 1](#).

To address stakeholders' concerns (including those of the AUASB), the following changes have been made to ISQM 1:

- (a) The taskforce agreed that a principles-based approach focusing on proactive and timely communication whatever the form, is the most appropriate. Reference to transparency reports is now in the application material (moved from a requirement) and is one of several examples of forms of communication to external parties.

15 *Evaluating the System of Quality Management (SOQM)*

In the submission on ED-ISQM 1, the AUASB raised a concern in relation to an annual evaluation of the SOQM, noting that an annual evaluation could be onerous particularly for SMPs or sole practitioners. The ISQM 1 taskforce noted that this concern was raised by multiple stakeholders, however, the taskforce is of the view that a cyclical evaluation would not achieve the intended purpose of the requirement, i.e., that leadership is aware and conscious of the effectiveness of their SOQM. The taskforce notes that the way leadership of an SMP may evaluate the SOQM is likely to be less

complex, and this has been emphasized in the example given in the application material paragraph A209C.

In relation to evaluating the SOQM, the AUASB is directed to the requirements in paragraphs 65A-65D of the [updated proposed ISQM 1](#).

To address stakeholders' concerns (including those of the AUASB), the following changes have been made to ISQM 1:

- (a) Including that the evaluation is taken at a point in time – application material A209B has been included to provide examples of the point in time when the evaluation may be undertaken.
- (b) Application material A210A has been added to explain the matters that may be considered by leadership in concluding on the SOQM including: severity and pervasiveness of identified deficiencies, whether the deficiencies have been remediated (or how being addressed), whether the effect of the deficiencies have been corrected. It is intended that leadership considers the combination of these matters.

16 *General scalability of the standard*

Overall comments from the AUASB in the submission on ED-ISQM 1 demonstrated concern for the scalability of the standard. In addition to the changes referred to throughout this paper, the ISQM 1 taskforce has made the following additional amendments to assist with salacity of the standard:

- (a) Signposting scalability examples in application material;
- (b) With the examples in the application material, including examples that address less complex and more complex firms to demonstrate the 'scaling up' and 'scaling down'.

17 *Documentation*

Overall comments from the AUASB in the submission on ED-ISQM 1 demonstrated concern for the extent of documentation that may be required by the standard. In relation to documentation, the AUASB is directed to the requirements in paragraphs 66-69 of the [updated proposed ISQM 1](#).

To address stakeholders' concerns (including those of the AUASB), the following changes have been made to ISQM 1:

- (a) Application material paragraph A212 enhances the emphasis in the standard on the need for professional judgement in determining documentation. A212 describes factors that may affect the firm's judgements about the form, content and extent of documentation including how often documentation is updated.
- (b) A214 clarifies that the firm is not required to document every factor that was considered in identifying and assessing quality risks.

Question 7: Are AUASB members comfortable with the way in which documentation has been addressed?

D. Other Matters to Raise for the AUASB's attention/comment:

- 18 Governance and Leadership component The AUASB is directed to the requirements in paragraph 23 of the [updated proposed ISQM 1](#).

Paragraph A29 has been revised to explain how the firm's business model may influence incentive structures and impact on quality.

Question 8: Are AUASB members comfortable with the revisions to paragraph A29?

E. The way forward:

The IAASB has indicated that the timing for approval of the quality management standards is expected June 2020.

Agenda Item 4–A

PROPOSED INTERNATIONAL STANDARD ON QUALITY MANAGEMENT 1 (PREVIOUSLY INTERNATIONAL STANDARD ON QUALITY CONTROL 1) – QUALITY MANAGEMENT FOR FIRMS THAT PERFORM AUDITS OR REVIEWS OF FINANCIAL STATEMENTS, OR OTHER ASSURANCE OR RELATED SERVICES ENGAGEMENTS

(Effective as of TBD)

(CLEAN)

CONTENTS

[Content Page to be Inserted]

Proposed International Standard on Quality Management (ISQM) 1, *Quality Management for Firms that Perform Audits or Reviews of Financial Statements, or Other Assurance or Related Services Engagements*, should be read in conjunction with the *Preface to the International Quality Management, Auditing, Review, Other Assurance, and Related Services Pronouncements*.

Introduction	Application and Other Explanatory Material
Scope of this ISQM	Scope of this ISQM (Ref: Para. 2)
1. This International Standard on Quality Management (ISQM) deals with a firm’s responsibilities to design, implement and operate a system of quality management for audits or reviews of financial statements, or other assurance or related services engagements. ISQM 2 ¹ deals with the responsibility of the firm and engagement quality reviewers relating to engagement quality reviews. This ISQM	

¹ Proposed ISQM 2, *Engagement Quality Reviews*

<p>is to be read in conjunction with relevant ethical requirements.</p>	
<p>2. Other pronouncements of the International Auditing and Assurance Standards Board (IAASB):</p> <p>(a) Are premised on the basis that the firm is subject to the ISQMs or to national requirements that are at least as demanding;² and</p> <p>(b) Include requirements for engagement partners and other personnel regarding quality management at the engagement level. ISA 220 (Revised), for example, deals with the specific responsibilities of the auditor regarding quality management at the engagement level for an audit of financial statements and the related responsibilities of the engagement partner. (Ref: Para. A1)</p>	<p>A1. Other pronouncements of the IAASB, including ISRE 2400 (Revised)³ and ISAE 3000 (Revised),⁴ also establish requirements for the engagement partner for the management of quality at the engagement level.</p>
<p>3. Law, regulation or relevant ethical requirements may establish responsibilities for the firm's management of quality beyond those described in this ISQM.</p>	
<p>4. This ISQM applies to all firms performing audits or reviews of financial statements, or other assurance or related services engagements (i.e., if the firm</p>	

² See, for example, Proposed International Standard on Auditing (ISA) 220 (Revised), *Quality Management for an Audit of Financial Statement* (Revised), paragraph 3

³ International Standard on Review Engagements (ISRE) 2400 (Revised), *Engagements to Review Historical Financial Statements*

⁴ International Standard on Assurance Engagements (ISAE) 3000 (Revised), *Assurance Engagements Other than Audits or Reviews of Historical Financial Information*

<p>performs any of these engagements, this ISQM applies).</p>	
<p>The Firm's System of Quality Management</p>	<p>The Firm's System of Quality Management (Ref: Para. 6A–13)</p>
<p>6A. A system of quality management is continual and iterative and is responsive to changes in the nature and circumstances of the firm and its engagements. It also does not operate in a linear manner. However, for the purposes of this ISQM, a system of quality management addresses the following eight components: (Ref: Para. A1A)</p> <ul style="list-style-type: none"> (a) The firm's risk assessment process; (b) Governance and leadership; (c) Relevant ethical requirements; (d) Acceptance and continuance of client relationships and specific engagements; (e) Engagement performance; (f) Resources; (g) Information and communication; and (h) The monitoring and remediation process. 	<p>A1A. The firm may use different terminology or frameworks to describe the components of its system of quality management.</p>
<p>7. The public interest is served by the consistent performance of quality engagements. Quality engagements are achieved through planning and performing engagements and reporting on them in accordance with professional standards and</p>	<p>A2. The IESBA Code⁵ contains requirements and application material for professional accountants that enable professional accountants to meet their responsibility to act in the public interest. In the context of engagement performance as described in this ISQM, the consistent performance of quality engagements forms part of the professional accountant's responsibility to act in the public interest.</p>

⁵ The International Ethics Standards Board for Accountants' *International Code of Ethics for Professional Accountants (including International Independence Standards)* (IESBA Code)

<p>applicable legal and regulatory requirements. Achieving the objectives of those standards and complying with the requirements of applicable law or regulation involves exercising professional judgment and, when applicable to the type of engagement, exercising professional skepticism. (Ref: Para. A2)</p>	
<p>8A. The system of quality management supports the consistent performance of quality engagements by providing the firm with reasonable assurance that the objectives of the system of quality management, stated in paragraph 18(a) and (b), are achieved. Since the system of quality management supports the consistent performance of quality engagements, in this ISQM, references to the design, implementation and operation of the system of quality management include supporting the performance of engagements. (Ref: Para. A3)</p>	<p>A3. Reasonable assurance is obtained when the system of quality management reduces to an acceptably low level the risk that the objectives stated in paragraph 18(a) and (b) are not achieved. Reasonable assurance is not an absolute level of assurance, because there are inherent limitations of a system of quality management. Such limitations include that human judgment in decision making can be faulty and that breakdowns in a system of quality management may occur, for example, due to human error or behavior or failures in IT applications.</p>
<p>9A. This ISQM requires the firm to apply a risk-based approach in designing, implementing and operating the components of the system of quality management in an interconnected and coordinated manner such that the quality of engagements is proactively managed by the firm. (Ref: Para. A4A)</p>	<p>A4A. Examples of the interconnected nature of the components include the following:</p> <ul style="list-style-type: none"> • The firm’s risk assessment process sets out the process the firm is required to follow in implementing the risk-based approach to quality management, and applies across the system of quality management. • The governance and leadership component provides the basis for the system of quality management and also creates the environment in which the other components of the system of quality management operate. • The information and communication and resources components enable the design, implementation and operation of the system of quality management. • The monitoring and remediation process is a process designed to monitor the entire system of quality management. The results of the monitoring and

	<p>remediation process may provide information that is relevant to the firm's risk assessment process.</p> <ul style="list-style-type: none">• There may be interrelationships of specific matters, for example, aspects of relevant ethical requirements may be relevant when accepting and continuing client relationships and specific engagements.
<p>10. The risk-based approach is embedded in the requirements of this ISQM through:</p> <p>(a) Establishing quality objectives. The quality objectives established by the firm consist of objectives in relation to the components of the system of quality management that are to be achieved by the firm. The firm is required to establish the quality objectives set out in this ISQM and any additional quality objectives beyond those specified by this ISQM that are considered necessary by the firm to achieve the objectives of the system of quality management.</p> <p>(b) Identifying and assessing risks to the achievement of the quality objectives (referred to in this standard as quality risks). The firm is required to identify and assess quality risks to provide a basis for designing and implementing responses.</p> <p>(c) Designing and implementing responses to address the assessed quality risks. The nature, timing and extent of the firm's responses to address the assessed quality risks are based on, and responsive to, the</p>	

<p>reasons for the assessments given to the quality risks.</p>	
<p>11A. This ISQM requires that, at least annually, the individual assigned ultimate responsibility and accountability for the system of quality management evaluates the system of quality management and concludes whether the system of quality management provides the firm with reasonable assurance that the objectives of the system are being achieved.</p>	
<p><i>Scalability</i></p> <p>13A. In applying a risk-based approach, the firm is required to take into account:</p> <ul style="list-style-type: none"> (a) The nature and circumstances of the firm; and (b) The nature and circumstances of the engagements performed by the firm. <p>Accordingly, the design of the firm’s system of quality management, in particular the complexity and formality of the system, will vary. For example, a firm that performs different types of engagements for a wide variety of entities, including audits of financial statements of listed entities, will likely need to have a more complex and more formal system of quality management than a firm that performs only reviews of financial statements or compilation engagements.</p>	
<p><i>Networks and Service Providers</i></p> <p>14. A firm’s system of quality management may include:</p>	

<p>(a) Network requirements or network services in circumstances when the firm belongs to a network; or</p> <p>(b) Resources that are obtained from a service provider that are external to the firm or external to the network when the firm belongs to a network.</p> <p>Notwithstanding the firm's responsibility to comply with network requirements, or the use of network services or resources from a service provider, the firm remains responsible for its system of quality management. Accordingly, this ISQM addresses the firm's responsibility in circumstances when the system of quality management includes network requirements or network services or resources from a service provider.</p>	
<p>Authority of this ISQM</p>	<p>Authority of this ISQM (Ref: Para. 16)</p>
<p>16. This ISQM contains the objective of the firm in following this ISQM, 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 and introductory material that provides context relevant to a proper understanding of this ISQM, and definitions. (Ref: Para. A6–A9)</p>	<p>A6. The objective of this ISQM provides the context in which the requirements of this ISQM are set, establishes the desired outcome of this ISQM and is intended to assist the firm in understanding what needs to be accomplished and, where necessary, the appropriate means of doing so.</p> <p>A7. The requirements of this ISQM are expressed using “shall.”</p> <p>A8. Where necessary, the application and other explanatory material provides further explanation of the requirements and guidance for carrying them out. In particular, it may:</p> <ul style="list-style-type: none"> • Explain more precisely what a requirement means or is intended to cover; and • Include examples that illustrate how the requirements might be applied.

	<p>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 ISQM. Where appropriate, additional considerations specific to public sector audit organizations are included within the application and other explanatory material. These additional considerations assist in the application of the requirements in this ISQM. They do not, however, limit or reduce the responsibility of the firm to apply and comply with the requirements in this ISQM.</p> <p>A9. This ISQM includes, under the heading “Definitions,” a description of the meanings attributed to certain terms for purposes of this ISQM. These definitions are provided to assist in the consistent application and interpretation of this ISQM, 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 <i>Handbook of International Quality Management, Auditing, Review, Other Assurance, and Related Services Pronouncements</i> published by IFAC includes the terms defined in this ISQM. The Glossary of Terms also includes descriptions of other terms found in the ISQMs to assist in common and consistent interpretation and translation.</p>
<p>Effective Date</p>	
<p>17. Systems of quality management in compliance with this ISQM are required to be designed, implemented, and commence operation by TBD.</p>	
<p>Objective</p>	
<p>18. The objective of the firm is to design, implement and operate a system of quality management for audits or reviews of financial statements, or other assurance or related services engagements</p>	

<p>performed by the firm, that provides the firm with reasonable assurance that:</p> <p>(a) The firm and its personnel fulfill their responsibilities in accordance with professional standards and applicable legal and regulatory requirements, and conduct engagements in accordance with such standards and requirements; and</p> <p>(b) Engagement reports issued by the firm or engagement partners are appropriate in the circumstances.</p>	
<p>Definitions</p>	<p>Definitions</p>
<p>19. In this ISQM, the following terms have the meanings attributed below:</p>	
<p>(a) Deficiency in the firm’s system of quality management (referred to as “deficiency” in this ISQM) – An aspect of the firm’s system of quality management that is absent, inappropriately designed, or not operating effectively. (Ref: Para. A9A–A10A, A175)</p>	<p><i>Deficiencies</i> (Ref: Para. 19(a))</p> <p>A9A. The firm identifies deficiencies through evaluating findings. A deficiency may arise from a finding, or a combination of findings.</p> <p>A10. An aspect of the system of quality management consists of quality objectives, quality risks and responses or other actions by the firm that are necessary to fulfill the requirements of this ISQM. As a result, a deficiency may exist in the design, implementation or operation of any of the components of the system of quality management.</p> <div style="border: 1px solid black; padding: 5px; margin-top: 10px;"> <p><i>Examples of an aspect of the firm’s system of quality management that is absent, inappropriately designed, or not operating effectively</i></p> <ul style="list-style-type: none"> • The individual(s) assigned ultimate responsibility and accountability for the system of quality management does not appropriately fulfill their </div>

		<p>responsibilities, including undertaking the annual evaluation of the system of quality management.</p> <ul style="list-style-type: none">• The firm's risk assessment process:<ul style="list-style-type: none">○ Is not designed or implemented in a manner that enables the firm to establish quality objectives, identify and assess quality risks and design and implement responses; or○ Fails to identify information that may affect the quality objectives, quality risks or responses.• A quality objective required to achieve the objective of this ISQM is not established. This may cause a quality risk to not be identified or properly assessed or a response to not be properly designed or implemented.• A quality risk has not been identified or properly assessed, such that a response that addresses that risk has not been properly designed or implemented.• A response to address an assessed quality risk is not properly designed, implemented or operating effectively, such that a quality objective may not be achieved. A response to address an assessed quality risk is not properly designed when, for example, a response necessary to address an assessed quality risk is absent or a response is not properly designed in a manner that effectively addresses an assessed quality risk.• The firm's monitoring and remediation process is not designed or implemented in a manner that:<ul style="list-style-type: none">○ Provides relevant, reliable and timely information about the design, implementation and operation of the system of quality management.○ Enables the firm to take appropriate actions to respond to identified deficiencies such that deficiencies are remediated on a timely basis.
--	--	---

	A10A. In some circumstances, an external oversight authority may establish requirements or guidance that set out matters that may be considered a deficiency.
(b) 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 ⁶ – The partner or other individual, appointed by the firm, who is responsible for the engagement and its performance, and for the report that is issued on behalf of the firm, and who, where required, has the appropriate authority from a professional, legal or regulatory body.	
(d) Engagement quality review – [To be aligned to ISQM 2]	
(e) Engagement quality reviewer – [To be aligned to ISQM 2]	
(f) Engagement team – [To be aligned to ISA 220 (Revised)]	
(g) External inspections – Inspections or investigations undertaken by an external oversight authority related to the firm’s system	<i>External Inspections</i> (Ref: Para. 19(g)) A11. In some circumstances, an external oversight authority may undertake other types of reviews.

⁶ “Engagement partner” and “partner” should be read as referring to their public sector equivalents where relevant.

<p>of quality management or engagements performed by the firm. (Ref: Para. A11)</p>	<p><i>Example of another type of review undertaken by an external oversight authority</i></p> <p>Thematic reviews of specific areas of focus that cross multiple audit firms, which are focused on matters that contribute to the improvement of engagement quality.</p>
<p>(gA) Findings (in relation to a system of quality management) – Information about the design, implementation and operation of the system of quality management, which comprises:</p> <p>(i) The results of the firm’s monitoring activities and external inspections; and</p> <p>(ii) Other information that indicates that one or more deficiencies may exist.</p>	
<p>(h) Firm – A sole practitioner, partnership or corporation or other entity of professional accountants, or public sector equivalent. (Ref: Para. A12)</p>	<p><i>Firm</i> (Ref: Para. 19(h))</p> <p>A12. The definition of “firm” in relevant ethical requirements may differ from the definition set out in this ISQM.</p>
<p>(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.</p>	
<p>(j) Network firm – A firm or entity that belongs to a network.</p>	

<p>(k) Network⁷ – A larger structure: (Ref: Para. A13–A14)</p> <p>(i) That is aimed at cooperation, and</p> <p>(ii) That is clearly aimed at profit or cost-sharing or shares common ownership, control or management, common quality management policies or procedures, common business strategy, the use of a common brand name, or a significant part of professional resources.</p>	<p><i>Network</i> (Ref: Para. 19(k), 58)</p> <p>A13. Networks and the firms within the network may be structured in a variety of ways. In some instances, network firms may provide services (e.g., resources) that are used by the firm in its system of quality management. There may also be circumstances when the network includes other structures or organizations that establish requirements for the firm related to its system of quality management, or provides services. For the purposes of this ISQM, networks and the other firms within the network are external to the firm and any network requirements or network services that are obtained from the network, network firms or another structure or organization in the network are considered “network requirements or network services.” Services used by the firm in the system of quality management that are obtained from outside of the network, network firms or another structure or organization in the network are considered services obtained from “service providers.”</p> <p>A14. The IESBA Code provides guidance in relation to the terms “network” and “network firm.”</p>
<p>(l) Partner – Any individual with authority to bind the firm with respect to the performance of a professional services engagement.</p>	
<p>(n) Professional judgment – The application of relevant training, knowledge and experience, within the context of professional standards, in making informed decisions about the courses of action that are appropriate in the design, implementation and operation of the firm’s system of quality management.</p>	

⁷ As defined in the IESBA Code

<p>(o) Professional standards – IAASB Engagement Standards, as defined in the IAASB’s <i>Preface to the International Quality Management, Auditing, Review, Other Assurance and Related Services Pronouncements</i>, and relevant ethical requirements.</p>	
<p>(p) Quality objectives – The desired outcomes in relation to the components of the system of quality management to be achieved by the firm.</p>	
<p>(q) Quality risks – Risks that have a reasonable possibility, individually or in combination with other quality risks, of:</p> <ul style="list-style-type: none"> (i) Occurring (i.e., likelihood); and (ii) Adversely affecting the achievement of a quality objective(s) if the risk were to occur (i.e., magnitude). 	
<p>(r) Reasonable assurance – In the context of the ISQMs, a high, but not absolute, level of assurance.</p>	
<p>(s) Relevant ethical requirements – Principles of professional ethics and ethical requirements that are applicable to professional accountants when undertaking engagements that are audits or reviews of financial statements or other assurance or related services engagements. Relevant ethical</p>	<p><i>Relevant Ethical Requirements</i> (Ref: Para. 19(s), 32)</p> <p>A15. The relevant ethical requirements that are applicable in the context of a system of quality management may vary, depending on the nature and circumstances of the firm and its engagements. The term “professional accountant” may be defined in relevant ethical requirements. For example, the IESBA Code defines the term “professional accountant” and further explains the scope of provisions in the IESBA</p>

<p>requirements ordinarily comprise the provisions of the IESBA Code related to audits or reviews of financial statements, or other assurance or related services engagements, together with national requirements that are more restrictive. (Ref: Para. A15–A16A, A67)</p>	<p>Code that apply to individual professional accountants in public practice and their firms.</p> <p>A16. The IESBA Code addresses circumstances when law or regulation precludes the professional accountant from complying with certain parts of the IESBA Code. It further acknowledges that some jurisdictions might have provisions in law or regulation that differ from or go beyond those set out in the IESBA Code and that professional accountants in those jurisdictions need to be aware of those differences and comply with the more stringent provisions, unless prohibited by law or regulation.</p> <p>A16A. Various provisions of the relevant ethical requirements may apply only to personnel in the context of performing engagements and not the firm itself. The firm’s system of quality management may need to address personnel’s compliance with such relevant ethical requirements.</p> <div data-bbox="982 722 1948 1372" style="border: 1px solid black; padding: 10px;"><p><i>Examples of relevant ethical requirements that are applicable only to personnel and not the firm, and which relate to the performance of engagements</i></p><p>Part 2 of the IESBA Code applies to individuals who are professional accountants in public practice when performing professional activities pursuant to their relationship with the firm, whether as a contractor, employee or owner. Part 2 of the IESBA Code addresses:</p><ul style="list-style-type: none">• Pressure to breach the fundamental principles, and includes requirements that an individual shall not:<ul style="list-style-type: none">○ Allow pressure from others to result in a breach of compliance with the fundamental principles; or○ Place pressure on others that the accountant knows, or has reason to believe, would result in the other individuals breaching the fundamental principles.<p>In the context of performing engagements, pressure to breach the fundamental principles may arise when an engagement partner or another</p></div>
--	--

		<p>senior member of the engagement team pressures an engagement team member or the engagement quality reviewer to breach the fundamental principles.</p> <ul style="list-style-type: none"> • Preparation and presentation of information, and includes requirements for professional accountants when preparing and presenting information for clients or their firms and therefore applies to personnel performing a compilation engagement.
<p>(t) Response (in relation to a system of quality management) – Policies or procedures designed and implemented by the firm to address an assessed quality risk: (Ref: Para. A17–A18, A24S)</p> <p>(i) Policies are statements of what should, or should not, be done to address an assessed quality risk. Such statements may be documented, explicitly stated in communications or implied through actions and decisions.</p> <p>(ii) Procedures are actions to implement policies.</p>		<p><i>Response</i> (Ref: Para. 19(t))</p> <p>A17. Policies are implemented through the actions of personnel and other individuals whose actions are subject to the policies, or through their restraint from taking actions that would conflict with the firm’s policies.</p> <p>A18. Procedures may be mandated, through formal documentation or other communications, or may result from behaviors that are not mandated but are rather conditioned by the firm’s culture. Procedures may be enforced through the actions permitted by IT applications, or other aspects of the firm’s IT environment.</p>
<p>(u) Staff – Professionals, other than partners, including any experts the firm employs.</p>		
<p>(v) System of quality management – A system designed, implemented and operated by a firm to provide the firm with reasonable assurance that:</p> <p>(i) The firm and its personnel fulfill their responsibilities in accordance with</p>		

<p>professional standards and applicable legal and regulatory requirements, and conduct engagements in accordance with such standards and requirements; and</p> <p>(ii) Engagement reports issued by the firm or engagement partners are appropriate in the circumstances.</p>	
<p>Requirements</p>	
<p>Applying, and Complying with, Relevant Requirements</p>	<p>Applying, and Complying with, Relevant Requirements (Ref: Para. 21)</p>
<p>20. The individual(s) assigned ultimate responsibility and accountability for the firm's system of quality management, and the individual(s) assigned operational responsibility for the firm's system of quality management shall have an understanding of this ISQM, including the application and other explanatory material, to understand the objective of this ISQM and to apply its requirements properly.</p>	
<p>21. The firm shall comply with each requirement of this ISQM unless the requirement is not relevant to the firm because of the nature and circumstances of the firm or its engagements. (Ref: Para. A20)</p>	<p>A20. <i>Examples of when a requirement of this ISQM may not be relevant to the firm</i></p> <ul style="list-style-type: none"> • The firm is a sole practitioner. For example, the requirements addressing the organizational structure and assigning roles, responsibilities and authority within the firm, direction, supervision and review and addressing differences of opinion may not be relevant. • The firm only performs engagements that are related services engagements. For example, if the firm is not required to maintain independence for the related services engagements, the requirement to

	<p>obtain a documented confirmation of compliance with independence requirements from all personnel would not be relevant.</p>
<p>System of Quality Management</p>	<p>System of Quality Management</p>
<p>22. The firm shall design, implement and operate a system of quality management. In doing so, the firm shall exercise professional judgment, taking into account the nature and circumstances of the firm and its engagements. The governance and leadership component of the system of quality management establishes the environment that supports the operation of the system of quality management, through the firm’s culture, decision-making processes, actions, organizational structure and leadership. (Ref: Para. A21A–A24)</p>	<p><i>Design, Implement and Operate a System of Quality Management</i> (Ref: Para. 22)</p> <p>A21A. Quality management is not a separate function of the firm; it is the integration of a quality culture and policies or procedures into the firm’s operational activities and processes with the purpose of actively managing quality. As a result, designing the system of quality management and the firm’s operational activities and processes in a unified manner may promote a harmonious approach to managing the firm, and enhance the effectiveness of quality management.</p> <p>A22A. Notwithstanding that the firm assigns roles and responsibilities related to the system of quality management, the firm remains ultimately responsible, and therefore accountable, for compliance with the requirements of this ISQM.</p> <p>A24. The quality of professional judgments exercised by the firm is likely to be enhanced when individuals making such judgments demonstrate an attitude that includes an inquiring mind, including:</p> <ul style="list-style-type: none"> • Being open and alert for situations and information (or the lack thereof) regarding the system of quality management, including factors related to the nature and circumstances of the firm and engagements it performs; and • Critically evaluating information obtained in formulating decisions about the system of quality management.
<p><i>Responsibilities</i></p> <p>22A. The firm shall assign: (Ref: Para. A24A–A24B)</p> <p>(a) Ultimate responsibility and accountability for the system of quality management to the firm’s chief executive officer or the firm’s</p>	<p><i>Responsibilities</i> (Ref: Para. 22A–22AA)</p> <p>A24A. The governance and leadership component includes a quality objective that the firm has an organizational structure with appropriate assignment of roles, responsibilities and authority..</p>

<p>managing partner (or equivalent) or, if appropriate, the firm’s managing board of partners (or equivalent).</p> <p>(b) Operational responsibility for the system of quality management.</p>	<p>A24B. How the firm assigns roles, responsibilities and authority within the firm may vary and law or regulation may impose certain requirements for the firm that affect the leadership and management structure or their assigned responsibilities.</p> <div style="border: 1px solid black; padding: 5px; margin: 10px 0;"> <p><i>Scalability example to demonstrate how assigning roles and responsibilities may be undertaken in a less complex firm</i></p> <p>In a less complex firm, ultimate responsibility and accountability for the system of quality management may be assigned to a single managing partner with sole responsibility for the oversight of the firm. This individual may also assume responsibility for all aspects of the system of quality management, including operational responsibility for the system of quality management, compliance with independence requirements and the monitoring and remediation process.</p> </div>
<p>22AA. In assigning operational responsibility for the system of quality management, and any other responsibilities for specific aspects of the system of quality management, the firm shall determine that the assigned individual(s) has: (Ref: Para. A24C–A24D)</p> <p>(a) The appropriate experience and knowledge and sufficient time to fulfill their assigned responsibility; and</p> <p>(b) An understanding of their assigned responsibility and accountability for such responsibility. (Ref: Para. A24E)</p>	<p>A24C. This ISQM also requires the firm to assign operational responsibility for compliance with independence requirements and the monitoring and remediation process.</p> <p>A24CA. The appropriate experience and knowledge for the individual assigned operational responsibility for the system of quality management may include:</p> <ul style="list-style-type: none"> • An understanding of the firm’s strategic decisions and actions and experience with the firm’s business operations; and • Having appropriate seniority, stature and influence within the firm. <p>A24D. An individual assigned operational responsibility for aspects of the system of quality management may further assign specific roles, procedures, tasks or actions to other individuals.</p> <p>A24E. Although an individual may be assigned responsibility for a particular aspect of the system of quality management, in order to fulfill their responsibility, the individual may need to understand how their role contributes to the system of quality management as a whole.</p>

<p>22B. The firm shall determine that the individual(s) assigned operational responsibility for the system of quality management has a direct line of communication to the individual(s) assigned ultimate responsibility and accountability for the system of quality management.</p>	
<p>The Firm's Risk Assessment Process</p>	<p>The Firm's Risk Assessment Process (Ref: Para. 22C–22G)</p>
<p>22C. The firm shall design and implement a risk assessment process to establish quality objectives, identify and assess quality risks to the achievement of the quality objectives and design and implement responses to address the assessed quality risks. (Ref: Para. A24F–A24H)</p>	<p>A24F. How the firm designs the firm's risk assessment process may be affected by the nature and circumstances of the firm, including how the firm is structured and organized. The firm's risk assessment process may be undertaken in relation to each component, or for the system of quality management as a whole.</p> <div data-bbox="982 667 1955 1255" style="border: 1px solid black; padding: 10px;"> <p><i>Scalability examples to demonstrate how the firm's risk assessment process may differ</i></p> <ul style="list-style-type: none"> • A less complex firm may have an informal risk assessment process, which is undertaken by the individual assigned operational responsibility for the system of quality management. • A more complex firm may have a more structured and formal risk assessment process, involving multiple individuals. The process may be centralized (e.g., the quality objectives, quality risks and responses are established centrally for all business units, functions and service lines) or decentralized (e.g., the quality objectives, quality risks and responses are established at a business unit, function or service line level, with the outputs combined at the firm level). The firm's network may also provide the firm with quality objectives, quality risks and responses to be included in the firm's system of quality management. </div> <p>A24G. The process of establishing quality objectives, identifying and assessing quality risks and designing and implementing responses is iterative.</p>

	<p><i>Examples of the iterative nature of the firm's risk assessment process</i></p> <ul style="list-style-type: none">• In identifying and assessing quality risks, the firm determines that a quality risk is also relevant to another quality objective(s).• When designing and implementing responses, the firm determines that a quality risk was not identified and assessed. <p>A24H. Information sources that enable the firm to establish quality objectives, identify and assess quality risks and design and implement responses form part of the firm's information and communication component. Information that is relevant to the firm's risk assessment process may be internal or external to the firm and may include:</p> <ul style="list-style-type: none">• Information about the factors that may affect the achievement of the quality objectives.• The results of the firm's monitoring and remediation process (see paragraph 49).• The results of external inspections.• Information available from other regulators, such as information from a securities regulator about an entity for whom the firm performs engagements (e.g., irregularities in their financial statements).• Changes in the system of quality management that affect other aspects of the system, for example, changes in the firm's resources.• Information from the network or service providers, including:<ul style="list-style-type: none">○ Information about network requirements or network services (see paragraph 58); and○ Other information from the network, including information about the results of monitoring activities undertaken by the network across the network firms (see paragraphs 60–61).
--	---

	<ul style="list-style-type: none"> • Other external sources, such as regulatory actions and litigation against the firm or other firms in the jurisdiction that may highlight areas for the firm to consider.
<p>22D. The firm shall establish the quality objectives specified by this ISQM and any additional quality objectives considered necessary by the firm to achieve the objectives of the system of quality management. (Ref: Para. A24I–A24K)</p>	<p><i>Establish Quality Objectives</i> (Ref: Para. 22D)</p> <div data-bbox="909 407 1955 609" style="border: 1px solid black; padding: 5px;"> <p>A24I. <i>Example of circumstances that may give rise to the need for additional quality objectives</i></p> <p>Law or regulation, or the requirements of national professional standards, require the firm to establish additional quality objectives.</p> </div> <p>A24J. The nature and circumstances of the firm and its engagements may be such that the objectives in this ISQM are considered complete, and the firm may not find it necessary to establish additional quality objectives.</p> <p>A24K. The firm may establish sub-objectives to enhance the firm’s identification and assessment of quality risks, and design and implementation of responses.</p>
<p>22E. The firm shall identify and assess quality risks to provide a basis for the design and implementation of responses. In doing so, the firm shall: (Ref: Para. A24L)</p> <p>(a) Understand the factors that may adversely affect the achievement of its quality objectives, including: (Ref: Para. A24N)</p> <p>(i) Those relating to the nature and circumstances of the firm:</p> <p>a. The complexity and operating characteristics of the firm;</p> <p>b. The strategic decisions, actions, and business model;</p>	<p><i>Identify and Assess Quality Risks</i> (Ref: Para. 22E)</p> <p>A24L. The identification of quality risks and assessment of quality risks may be undertaken separately or concurrently.</p> <p>A24N. The factors that may adversely affect the achievement of a quality objective consist of conditions, events, circumstances, actions or inactions. There may be factors in addition to those described in paragraph 22E(a) that may adversely affect the achievement of a quality objective.</p> <div data-bbox="966 1170 1955 1317" style="border: 1px solid black; padding: 5px;"> <p><i>Examples of factors that may be considered by the firm in determining whether they adversely affect the achievement of a quality objective</i></p> <p>Conditions and circumstances:</p> </div>

<p>c. The characteristics and management style of leadership;</p> <p>d. The resources of the firm, including the resources provided by service providers;</p> <p>e. Law, regulation, professional standards and the environment in which the firm operates; and</p> <p>f. In the case of a firm that belongs to a network, the characteristics of the network requirements and network services, if any.</p> <p>(ii) Those relating to the nature and circumstances of the engagements performed by the firm subject to the system of quality management:</p> <p>a. The types of engagements performed by the firm and the reports to be issued; and</p> <p>b. The types of entities for which such engagements are undertaken;</p> <p>(b) Consider:</p> <p>(i) Whether, and if so how, the factors could, individually or in combination with other quality risks, adversely affect the achievement of a quality objective; and (Ref: Para. A24P)</p>	<ul style="list-style-type: none"> • The size of the firm, the geographical dispersion of the firm, how the firm is structured or the extent to which the firm concentrates or centralizes its processes or activities (e.g., use of service delivery centers). • The services offered by the firm, including services not within the scope of this ISQM, and the relative significance of the various services to the firm's overall financial goals. • The composition of firm leadership and their tenure, and how authority is distributed among leadership. • Economic stability and social factors, and standards or regulation affecting engagements performed by the firm. • The nature of the firm's resources, how resources will be used in the firm's system of quality management, the firm's dependency on resources from service providers and the characteristics of the service providers used by the firm, and the resources they provide. • The nature of the network, how the network is organized and the nature and extent of the requirements established by the network or services provided by the network. <p>Actions or inactions:</p> <ul style="list-style-type: none"> • Decisions and actions taken by the firm in obtaining and allocating resources. • Decisions about financial and operational matters, including: <ul style="list-style-type: none"> ○ Commercial considerations; and ○ The firm's strategic goals. • How leadership motivates and encourages personnel. <p>Events:</p>
--	---

<p>(ii) The likelihood of the quality risks occurring, and if they were to occur the potential effect on the achievement of a quality objective(s) before consideration of any response. (Ref: Para. A24Q)</p>	<div data-bbox="968 191 1955 305" style="border: 1px solid black; padding: 5px;"> <ul style="list-style-type: none"> • Audit failures that affect the general public's perception of professional accountancy firms. </div> <p>A24P. Not every factor will affect every quality objective and therefore, not every factor will give rise to a quality risk in a component.</p> <p>A24Q. The assessment of identified quality risks need not comprise formal ratings or scores.</p> <div data-bbox="982 500 1955 846" style="border: 1px solid black; padding: 5px;"> <p><i>Examples of how the quality risks may be considered by the firm in assessing the potential effect on the achievement of a quality objective(s)</i></p> <ul style="list-style-type: none"> • How frequently the quality risk is expected to occur. • How much time it would take for the the quality risk to have an effect, and whether in that time the firm would have an opportunity to respond to mitigate the effect of the quality risk. • How long the quality risk would affect the firm once it has occurred. </div>
<p>22F. The firm shall design and implement responses to address the assessed quality risks in a manner that is based on, and responsive to, the reasons for the assessments given to the quality risks. In doing so, the firm shall include the responses specified by this ISQM in paragraph 41A. (Ref: Para. A24R – A24T)</p>	<p><i>Design and Implement Responses to Assessed Quality Risks</i> (Ref: Para. 22F)</p> <p>A24R. The nature, timing and extent of the responses are affected by the reasons for the assessment given to the quality risks, which includes:</p> <ul style="list-style-type: none"> • The likelihood of occurrence. • The effect on the achievement of a quality objective(s). The factors that may adversely affect the achievement of the quality objectives that give rise to the assessed quality risks. <p>A24S. The responses designed and implemented by the firm may operate at the firm level or engagement level, or there may be a combination of responsibilities for actions to be taken at the firm and engagement level.</p>

	<p><i>Example of a response that operates at both the firm and engagement level</i></p> <p>The firm establishes policies or procedures setting out specific matters for which consultation by engagement teams is required. The firm appoints suitably qualified and experienced individuals to provide technical advice to engagement teams. The engagement team is responsible for identifying when matters for consultation occur and initiating consultation.</p> <p>A24T. The need for formally documented policies or procedures may be greater for firms that have many personnel or that are geographically dispersed, in order to achieve consistency across the firm.</p>
<p><i>Modifications to the Quality Objectives, Quality Risks or Responses</i></p> <p>22G. The firm shall establish policies or procedures that are designed to identify information that may affect the quality objectives, quality risks or responses. The firm shall consider whether: (Ref: Para. A24VA–A24X)</p> <p>(a) Additional quality objectives need to be established and if so, shall establish them; and</p> <p>(b) The quality risks or responses require modification, and if so, shall modify them accordingly. (Ref: Para. A24Y)</p>	<p><i>Modifications to the Quality Objectives, Quality Risks or Responses (Ref: Para. 22G)</i></p> <p><i>A24VA. Scalability example to demonstrate how the policies or procedures designed to identify information that may affect the quality objectives, quality risks or responses may vary</i></p> <ul style="list-style-type: none"> • In a less complex firm, the individuals responsible for establishing quality objectives, identifying and assessing quality risks and designing and implementing responses may, in the normal course of their activities, be aware of information that may affect the quality objectives, quality risks and responses. In such cases, the firm’s policies or procedures may be informal. • In a more complex firm, the firm may need to establish formal policies or procedures to identify information that may affect the quality objectives, quality risks or responses. This may include a periodic review of information relating to the nature and circumstances of the firm and engagements it performs, environmental scans or risk sensing. <p>A24W. Changes in the nature and circumstances of the firm’s engagements may affect the design, implementation and operation of the system of quality management.</p>

	<p><i>Example of how a change in the nature and circumstances of the firm's engagements may affect the design, implementation and operation of the system of quality management</i></p> <p>The firm accepts an engagement to perform an audit of financial statements for an entity involved in an industry for which the firm has not previously performed audit engagements. This gives rise to new quality risks, including that individuals do not have the knowledge or experience relevant to the engagement.</p> <p>A24X. Additional quality objectives may need to be established, or quality risks and responses modified as part of the remedial actions undertaken by the firm to address a deficiency in accordance with paragraph 49.</p> <p>A24Y. Modifications to quality risks or responses include adjusting an assessed quality risk, reassessing a quality risk, identifying a new quality risk, adjusting the design or implementation of a response, or designing and implementing a new response.</p>
<p>Governance and Leadership</p>	<p>Governance and Leadership</p>
<p>23. The firm shall establish the following quality objectives that address the aspects of the firm's environment that support the design, implementation and operation of the system of quality management:</p> <p>(a) The firm commits to quality and a culture of quality exists throughout the firm, including recognizing and reinforcing: (Ref: Para. A26–A29)</p> <p>(i) The firm's role in serving the public interest by consistently performing quality engagements;</p>	<p><i>Culture</i> (Ref: Para. 23(a))</p> <p>A26. The firm's culture is an important factor in influencing the behavior of personnel and other individuals. Relevant ethical requirements ordinarily establish the principles of professional ethics, and are further addressed in the relevant ethical requirements component of this ISQM.</p> <p><i>Examples of professional values and attitudes</i></p> <ul style="list-style-type: none"> • Professional manner, for example, timeliness, courteousness, respect, accountability, responsiveness, and dependability. • A commitment to teamwork. • Maintaining an open mind to new ideas or different perspectives in the professional environment.

<p>(ii) The importance of professional ethics, values and attitudes;</p> <p>(iii) The responsibility of all individuals for quality relating to the performance of engagements or activities within the system of quality management, and their expected behavior; and</p> <p>(iv) The importance of quality in the firm's strategic decisions and actions, including the firm's financial and operational priorities.</p> <p>(b) Leadership is responsible and accountable to the firm for quality. (Ref: Para. A29A)</p> <p>(c) Leadership demonstrates a commitment to quality through their actions and behaviors. (Ref: Para. A30A)</p> <p>(d) The organizational structure and assignment of roles, responsibilities and authority is appropriate to enable the design, implementation and operation of the firm's system of quality management. (Ref: Para. A31–A31A)</p> <p>(e) Resource needs, including financial resources, are planned for and resources are obtained, allocated or assigned in a manner that is consistent with the firm's commitment to quality. (Ref: Para. A34–A35)</p>	<div data-bbox="982 193 1955 412" style="border: 1px solid black; padding: 5px;"> <ul style="list-style-type: none"> • Pursuit of excellence. • A commitment to continual improvement (e.g., setting expectations beyond the minimum requirements and placing a focus on continual learning). • Social responsibility. </div> <p>A29. The firm's strategic decision-making process, including the establishment of a business strategy, may include matters such as the firm's decisions about financial and operational matters, the firm's financial goals, how financial resources are managed, growth of the firm's market share, industry specialization or new service offerings. The firm's financial and operational priorities may directly or indirectly affect the firm's commitment to quality and culture of quality.</p> <div data-bbox="982 667 1955 867" style="border: 1px solid black; padding: 5px;"> <p><i>Example of how the firm's financial and operational priorities may affect the firm's commitment to quality and culture of quality</i></p> <p>Incentives that are focused on financial and operational priorities may discourage behaviors that demonstrate a commitment to quality.</p> </div> <p><i>Leadership</i> (Ref: Para. 23(b) and 23(c))</p> <p>A29A. The responses designed and implemented by the firm to hold leadership responsible and accountable for quality include the performance evaluations required by paragraph 65D.</p> <p>A30A. Although leadership establishes the tone at the top through their actions and behaviors, clear, consistent and frequent actions and communications at all levels within the firm may be essential to promoting a culture of quality.</p> <p><i>Organizational Structure</i> (Ref: Para. 23(d))</p> <p>A31. The organizational structure of the firm may include operating units, operational processes, divisions or geographical locations and other structures. In some instances, the firm may concentrate or centralize processes or activities in a service</p>
---	--

	<p>delivery center, and engagement teams may include individuals from the service delivery center who perform specific tasks that are repetitive or specialized in nature.</p> <p>A31A. How the firm assigns roles, responsibilities and authority within the firm may vary.</p> <div style="border: 1px solid black; padding: 10px; margin: 10px 0;"> <p><i>Scalability examples to demonstrate how assigning roles and responsibilities may vary</i></p> <ul style="list-style-type: none"> • In a less complex firm, the individual with oversight of the firm may assume all of the roles and responsibilities related to the system of quality management. • In a more complex firm, there may be multiple levels of leadership that reflect the organizational structure of the firm, and the firm may have an independent governing body that has non-executive oversight of the firm, which may comprise external individuals. </div> <p><i>Resources (Ref: Para. 23(e))</i></p> <p>A34. The individuals(s) assigned ultimate responsibility and accountability or operational responsibility for the system of quality management are in most cases able to influence the nature and extent of resources that the firm obtains, develops, uses and maintains, and how those resources are allocated or assigned, including the timing of when they are used.</p> <p>A35. Resource needs may change over time, however it may not be practicable to anticipate all resource needs. The firm's resource planning may involve determining the resources currently required, forecasting the firm's future resource needs, and establishing processes to deal with unanticipated resource needs when they arise.</p>
<p>Relevant Ethical Requirements</p>	<p>Relevant Ethical Requirements (Ref: Para. 32)</p>
<p>32. The firm shall establish the following quality objectives that address the fulfillment of responsibilities in accordance with relevant ethical</p>	<p>A67. The IESBA Code sets out the fundamental principles of ethics that establish the standard of behavior expected of a professional accountant and establishes the International Independence Standards. The fundamental principles are integrity, objectivity, professional competence and due care, confidentiality and professional</p>

<p>requirements, including those related to independence: (Ref: Para. A67– A68, A75)</p> <p>(a) The firm, its personnel and others subject to relevant ethical requirements, including, as applicable, the network, network firms, personnel in the network or network firms, or service providers:</p> <p>(i) Understand the relevant ethical requirements to which the firm and the firm’s engagements are subject. (Ref: Para. A15, A16A, A71)</p> <p>(ii) Fulfill their responsibilities in relation to the relevant ethical requirements to which the firm and the firm’s engagements are subject, including: (Ref: Para. A72–A74)</p> <p>a. Identifying, evaluating and addressing threats to compliance with the relevant ethical requirements; and</p> <p>b. Identifying, communicating, evaluating and reporting of any breaches of the relevant ethical requirements and appropriately responding to the causes and consequences of the breaches in a timely manner.</p>	<p>behavior. The IESBA Code also specifies the approach that a professional accountant is required to apply to comply with the fundamental principles and the International Independence Standards and addresses specific topics relevant to complying with the fundamental principles. Law or regulation in a jurisdiction may also contain provisions addressing ethical requirements, including independence (e.g., privacy laws affecting the confidentiality of information).</p> <p>A68. In some cases, the matters addressed by the firm in its system of quality management may be more specific than, or additional to, the provisions of relevant ethical requirements.</p> <div data-bbox="982 558 1948 945" style="border: 1px solid black; padding: 5px;"> <p><i>Examples of matters that a firm may include in its system of quality management that are more specific than, or additional to, the provisions of relevant ethical requirements</i></p> <ul style="list-style-type: none"> • The firm prohibits the acceptance of gifts and hospitality from a client, even if the value is trivial and inconsequential. • The firm sets rotation periods in addition to those specified in relevant ethical requirements, which apply to all engagement partners, including those performing other assurance or related services engagements, and all senior engagement team members. </div> <p>A71. The applicability of the relevant ethical requirements to others (e.g., the network, network firms, personnel in the network or network firms, or service providers) depends on the provisions of the relevant ethical requirements and how the firm uses others in its system of quality management, including in the performance of engagements.</p> <div data-bbox="968 1162 1948 1380" style="border: 1px solid black; padding: 5px;"> <p><i>Examples of relevant ethical requirements that apply to others</i></p> <ul style="list-style-type: none"> • Relevant ethical requirements may include requirements for independence that apply to network firms or employees of network firms, for example, the IESBA Code includes independence requirements that apply to a network firm. </div>
--	---

	<ul style="list-style-type: none">• The definition of engagement team under relevant ethical requirements may include any individuals engaged by the firm who perform assurance procedures on the engagement (e.g., a service provider engaged to attend a physical inventory count at a remote location). Accordingly, any requirements of the relevant ethical requirements that apply to the engagement team may also be relevant to such individuals.• The principle of confidentiality may apply to a network, network firm or service provider, given that they may have access to client information obtained by the firm. <p>A72. Relevant ethical requirements may contain provisions regarding the identification and evaluation of threats and how they should be addressed. For example, the IESBA Code provides a conceptual framework for this purpose and, in applying the conceptual framework, requires that the firm use the reasonable and informed third party test.</p> <p>A73. Matters that may need to be addressed by the firm relating to breaches of the relevant ethical requirements, include:</p> <ul style="list-style-type: none">• The communication of breaches of the relevant ethical requirements to appropriate individual(s) within the firm;• The evaluation of the significance of a breach and its effect on compliance with relevant ethical requirements;• The actions to be taken to satisfactorily address the consequences of a breach, including that such actions be taken as soon as practicable;• Determining whether to report a breach to external parties, such as those charged with governance of the entity to which the breach relates or an external oversight authority; and• Determining the appropriate actions to be taken in relation to the individual(s) responsible for the breach.
--	--

	<p>A74. Relevant ethical requirements may specify how the firm is required to respond to a breach. For example, the IESBA Code sets out requirements for the firm in the event of a breach of the IESBA Code and includes specific requirements addressing breaches of the International Independence Standards, which includes requirements for communication with external parties.</p> <p><i>Public Sector Considerations</i></p> <p>A75. In achieving the quality objectives in this ISQM related to independence, public sector auditors may have regard to the public sector mandate and statutory measures, and address independence in that context.</p>
<p>Acceptance and Continuance of Client Relationships and Specific Engagements</p>	<p>Acceptance and Continuance of Client Relationships and Specific Engagements</p>
<p>34. The firm shall establish the following quality objectives that address the acceptance and continuance of client relationships and specific engagements:</p> <p>(a) Judgments by the firm about whether to accept or continue a client relationship or specific engagement are appropriate based on:</p> <p>(i) Relevant information obtained about the nature and circumstances of the engagement and the integrity and ethical values of the client (including management, and, when appropriate, those charged with governance) that is sufficient to support such judgments; and (Ref: Para. A77–A82)</p>	<p><i>The Nature and Circumstances of the Engagement and the Integrity and Ethical Values of the Client</i> (Ref: Para. 34(a)(i))</p> <p>A77. The information obtained about the nature and circumstances of the engagement may include:</p> <ul style="list-style-type: none"> • The industry of the entity for which the engagement is being undertaken and relevant regulatory factors; • The nature of the entity, for example, its operations, organizational structure, ownership and governance, its business model and how it is financed; and • The nature of the underlying subject matter and the criteria.

<p>(ii) The firm's ability to perform the engagement in accordance with professional standards and applicable legal and regulatory requirements. (Ref: Para. A83)</p> <p>(b) The financial and operational priorities of the firm do not lead to inappropriate judgments about whether to accept or continue a client relationship or specific engagement. (Ref: Para. A85–A86)</p>	<p><i>Example of underlying subject matter and criteria</i></p> <p>In the case of integrated reporting:</p> <ul style="list-style-type: none"> • The underlying subject matter may include social, environmental and health and safety information; and • The criteria may be performance measures established by a recognized body of experts. <p>A79. The information obtained to support the firm's judgments about the integrity and ethical values of the client may include the identity and business reputation of the client's principal owners, key management, and those charged with its governance.</p> <p><i>Examples of factors that may affect the nature and extent of information obtained about the integrity and ethical values of the client</i></p> <ul style="list-style-type: none"> • The nature of the entity for which the engagement is being performed, including the complexity of its ownership and management structure. • The nature of the client's operations, including its business practices. • Information concerning the attitude of the client's principal owners, key management and those charged with its governance towards such matters as aggressive interpretation of accounting standards and the internal control environment. • Whether the client is aggressively concerned with maintaining the firm's fees as low as possible. • Indications of a client-imposed limitation in the scope of work. • Indications that the client might be involved in money laundering or other criminal activities. • The reasons for the proposed appointment of the firm and non-reappointment of the previous firm.
---	--

	<ul style="list-style-type: none">• The identity and business reputation of related parties. <p>A80. The firm may obtain the information from a variety of internal and external sources.</p> <p><i>Examples of sources of information about the integrity and ethical values of the client</i></p> <ul style="list-style-type: none">• In the case of an existing client, information from current or previous engagements, if applicable, or inquiry of other personnel who have performed other engagements for the client.• In the case of a new client, inquiry of existing or previous providers of professional accountancy services to the client, in accordance with relevant ethical requirements.• Discussions with other third parties, such as bankers, legal counsel and industry peers.• Background searches of relevant databases (which may be intellectual resources). In some cases, the firm may use a service provider to perform the background search. <p>A81. Information that is obtained during the firm’s acceptance and continuance process is in most cases also relevant to the engagement team when planning and performing the engagement. Professional standards may specifically require the engagement team to obtain or consider such information. For example, ISA 220 (Revised)⁸ requires the engagement partner to take into account information obtained in the acceptance and continuance process in planning and performing the audit engagement.</p> <p>A82. Professional standards or legal and regulatory requirements may include specific provisions that need to be addressed before accepting or continuing a client</p>
--	---

⁸ Proposed ISA 220 (Revised), paragraph 21

relationship or specific engagement and may also require the firm to make inquiries of an existing or predecessor firm when accepting an engagement. For example, when there has been a change of auditors, ISA 300⁹ requires the auditor, prior to starting an initial audit, to communicate with the predecessor auditor in compliance with relevant ethical requirements. The IESBA Code also includes requirements for the consideration of conflicts of interests in accepting or continuing a client relationship or specific engagement and communication with the existing or predecessor firm when accepting an engagement that is an audit or review of financial statements.

The Firm's Ability to Perform Engagements (Ref: Para. 34(a)(ii))

A83. The firm's ability to perform the engagement in accordance with professional standards and applicable legal and regulatory requirements may be affected by:

- The availability of appropriate resources to perform the engagement;
- Having access to information to perform the engagement, or to the persons who provide such information; and.
- Whether the firm, its personnel and other individuals involved in the engagement are able to fulfill their responsibilities in relation to the relevant ethical requirements.

Examples of factors the firm may consider in determining whether appropriate resources are available to perform the engagement

- The circumstances of the engagement and the reporting deadline.
- The availability of individuals with the appropriate competence and capabilities, including sufficient time, to perform the engagement. This includes:
 - Individuals to direct and supervise the engagement and take overall responsibility; and

⁹ ISA 300, *Planning an Audit of Financial Statements*, paragraph 13(b)

- Individuals with knowledge of the relevant industry or the underlying subject matter or criteria to be applied in the preparation of the subject matter information and experience with relevant regulatory or reporting requirements.
- The availability of experts, if needed.
- If an engagement quality review is needed, whether there is an individual available who meets the eligibility requirements in ISQM 2.
- The need for technological resources, for example, IT applications that enable the engagement team to perform procedures on the entity's data.
- The need for intellectual resources, for example, a methodology, industry or subject matter-specific guides, or access to information sources.

The Firm's Financial and Operational Priorities (Ref: Para. 34(b))

A85. Financial priorities may focus on the profitability of the firm, and fees obtained for the performance of engagements have an effect on the firm's financial resources. Operational priorities may include strategic focus areas, such as growth of the firm's market share, industry specialization or new service offerings. There may be circumstances when the firm is satisfied with the fee quoted for an engagement but, notwithstanding the firm's operational and financial priorities, it is not appropriate for the firm to accept or continue the engagement or client relationship (e.g., when the client lacks integrity and ethical values).

A86. There may be other circumstances when the fee quoted for an engagement is not sufficient given the nature and circumstances of the engagement, and it may diminish the firm's ability to perform the engagement in accordance with professional standards and applicable legal and regulatory requirements. The IESBA Code addresses fees and other types of remuneration, including circumstances that may create a threat to compliance with the fundamental principle of professional competence and due care if the fee quoted for an engagement is too low.

Engagement Performance	Engagement Performance
<p>36. The firm shall establish the following quality objectives that address the performance of quality engagements:</p> <p>(a) Engagement teams understand and fulfill their responsibilities in connection with the engagements, including, as applicable, the overall responsibility of the engagement partners for managing and achieving quality on the engagement and being sufficiently and appropriately involved throughout the engagement. (Ref: Para. A92)</p> <p>(b) The nature, timing and extent of direction and supervision of engagement teams and review of the work performed is appropriate based on the nature and circumstances of the engagements and the resources assigned or made available to the engagement teams, and the work performed by less experienced members of the engagement teams is directed, supervised and reviewed by more experienced engagement team members. (Ref: Para. A93–A93A)</p> <p>(c) Engagement teams exercise appropriate professional judgment and, when applicable to the type of engagement, professional skepticism. (Ref: Para. A96)</p> <p>(d) Consultation on difficult or contentious matters is undertaken and the conclusions</p>	<p><i>Responsibilities of the Engagement Team and Direction, Supervision and Review</i> (Ref: Para. 36(a) and 36(b))</p> <p>A92. The responsibilities of the engagement partner for managing and achieving quality on the engagement and for being sufficiently and appropriately involved throughout the engagement include responsibility for appropriate direction and supervision of the engagement team and review of the work performed.</p> <p>A93. <i>Examples of responsibilities for supervision and review</i></p> <ul style="list-style-type: none"> • Examples of responsibilities for supervision include: <ul style="list-style-type: none"> ○ Tracking the progress of the engagement; ○ Considering the competence and capabilities of individual members of the engagement team, whether they have sufficient time to carry out their work, whether they understand their instructions and whether the work is being carried out in accordance with the planned approach to the engagement; ○ Addressing matters arising during the engagement, considering their significance and modifying the planned approach appropriately; and ○ Identifying matters for consultation or consideration by more experienced engagement team members during the engagement. • Examples of responsibilities for review include consideration of whether: <ul style="list-style-type: none"> ○ The work has been performed in accordance with professional standards and applicable legal and regulatory requirements; ○ Significant matters have been raised for further consideration; ○ Appropriate consultations have been undertaken and the resulting conclusions have been documented and implemented;

<p>agreed are implemented. (Ref: Para. A98–A99A)</p> <p>(e) Differences of opinion within the engagement team, or between the engagement team and the engagement quality reviewer or personnel performing activities within the firm’s system of quality management are brought to the attention of the firm and resolved. (Ref: Para. A100)</p> <p>(f) Engagement documentation is assembled on a timely basis after the date of the engagement report, and is appropriately maintained and retained to meet the needs of the firm and comply with law, regulation, relevant ethical requirements, or other professional standards.(Ref: Para. A108–A111)</p>	<ul style="list-style-type: none"> ○ There is a need to revise the nature, timing and extent of work performed; ○ The work performed supports the conclusions reached and is appropriately documented; ○ The evidence obtained for an assurance engagement is sufficient and appropriate to support the report; and ○ The objectives of the engagement procedures have been achieved. <p><i>A93A. Examples of responsibilities for supervision and review</i></p> <p>In some circumstances, the firm may use a service delivery center and individuals from the service delivery center may be included in the engagement team. In such cases, the firm’s policies or procedures addressing direction, supervision and review may specify:</p> <ul style="list-style-type: none"> ● What aspects of the engagement may be assigned to individuals in the service delivery center; and ● How the engagement partner, or their designee, is expected to direct, supervise and review the work undertaken by individuals in the service delivery center. <p>The firm may also establish methods for communication between the engagement team and individuals in the service delivery center to facilitate direction, supervision and review of the work undertaken by individuals in the service delivery center.</p> <p><i>Professional Judgment and Professional Skepticism (Ref: Para. 36(c))</i></p> <p>A96. Professional skepticism supports the quality of judgments made on the engagement and, through these judgments, the overall effectiveness of the engagement team in performing the engagement. Other pronouncements of the IAASB may address the</p>
--	--

	<p>exercise of professional judgment or professional skepticism at the engagement level. For example, ISA 220 (Revised)¹⁰ explains the impediments to the exercise of professional skepticism at the engagement level and actions that the engagement partner may take to deal with such impediments.</p> <p><i>Consultation (Ref: Para. 36(d))</i></p> <p>A98. Consultation typically involves a discussion at the appropriate professional level, with individuals within or outside the firm who have specialized expertise, on difficult or contentious matters. An environment that reinforces the importance and benefit of consultation and encourages engagement teams to consult may contribute to supporting a firm culture that promotes a commitment to quality.</p> <p>A99. Difficult or contentious matters on which consultation is needed may either be specified by the firm, or the engagement team may identify matters that require consultation. The firm may also specify how conclusions should be agreed and implemented.</p> <p>A99A. ISA 220 (Revised)¹¹ includes requirements for the engagement partner related to consultation.</p> <p><i>Differences of Opinion (Ref: Para. 36(e))</i></p> <p>A100. The firm may encourage that differences of opinion are identified at an early stage, and may specify the steps to be taken in raising and dealing with them, including how the matter should be resolved, how the related conclusions should be implemented and conclusions documented. In some circumstances, resolving differences of opinion may be achieved through consulting with another practitioner or firm, or a professional or regulatory body.</p>
--	---

¹⁰ Proposed ISA 220 (Revised), paragraphs A27–A29

¹¹ Proposed ISA 220 (Revised), paragraph 32

Engagement Documentation (Ref: Para. 36(f))

A108. Law or regulation may prescribe the time limits by which the assembly of final engagement files for specific types of engagements is to be completed. Where no such time limits are prescribed in law or regulation, the time limit may be determined by the firm.

Example of time limit for assembly of final engagement files

The firm establishes policies or procedures for audits of financial statements that require engagement files to be assembled within 60 days after the date of the auditor's report.

A109. The retention and maintenance of engagement documentation may include managing the safe custody, integrity, accessibility or retrievability of the underlying data and the related technology. The retention and maintenance of engagement documentation may involve the use of IT applications. The integrity of engagement documentation may be compromised if it is altered, supplemented or deleted without authorization to do so, or if it is permanently lost or damaged.

A111. Law, regulation, relevant ethical requirements or other professional standards may prescribe the retention period for engagement documentation. If the retention periods are not prescribed, the firm may, in determining a retention period, consider the nature of the engagements performed by the firm and the firm's circumstances, including whether the engagement documentation is needed to provide a record of matters of continuing significance to future engagements.

Example of retention period for engagement documentation

The firm establishes policies or procedures for audits of financial statements that require engagement files to be retained for five years from the date of the auditor's report, or, if later, the date of the auditor's report on the group financial statements, when applicable.

Resources	Resources (Ref: Para. 38)
<p>38. The firm shall establish the following quality objectives that address appropriately obtaining, developing, using, maintaining, allocating and assigning resources, including resources from service providers, in a timely manner to enable the design, implementation and operation of the system of quality management: (Ref: Para. A113–A115)</p> <p>(a) Personnel are hired, developed and retained and have the competence and capabilities to: (Ref: Para. A117–A119)</p> <p>(i) Consistently perform quality engagements, including having knowledge or experience relevant to the engagements the firm performs; or</p> <p>(ii) Perform activities or carry out responsibilities in relation to the operation of the firm’s system of quality management.</p> <p>(b) Engagement team members are assigned to each engagement, including an engagement partner, who have appropriate competence and capabilities, including being given sufficient time, to consistently perform quality engagements. (Ref: Para. A120)</p> <p>(c) Individuals are assigned to perform activities within the system of quality management who have appropriate competence and</p>	<p>A113. Resources for the purposes of the resources component include:</p> <ul style="list-style-type: none"> • Human resources. • Technological resources, for example, IT applications. • Intellectual resources, for example, written policies or procedures, a methodology or guides. <p>A115. Resources may be internal to the firm, or may be obtained externally from a network, network firm or service provider:</p> <ul style="list-style-type: none"> • In circumstances when a resource is obtained from a service provider, the quality objectives in this component apply to the resource provided by the service provider. • In circumstances when a resource is obtained from a network or another network firm, the firm is required to comply with paragraphs 58–63 addressing network requirements or network services in achieving the objectives in this component. <div style="border: 1px solid black; padding: 10px; margin-top: 10px;"> <p><i>Example of how the quality objectives in this component are relevant to a resource obtained from a service provider</i></p> <p>The firm may use an IT application from a service provider. As a result, the quality objectives in paragraphs 38(e) and 38(g) apply to the resource. Furthermore, the use of the IT application from a service provider may also create the need for additional responses from the firm, including obtaining other resources, for example, the firm may need to have specific infrastructure to support the IT application or the firm may need to train individuals who will use the IT application so that it is used in the manner intended.</p> </div>

<p>capabilities, including sufficient time, to perform such activities. (Ref: Para. A120)</p> <p>(d) Personnel demonstrate a commitment to quality through their actions and behaviors, develop and maintain the appropriate competence to perform their roles, and are held accountable or recognized through timely evaluations, compensation, promotion and other incentives. (Ref: Para. A121–A123)</p> <p>(e) Appropriate technological resources are obtained or developed, implemented and maintained, and appropriately used, to enable the operation of the firm’s system of quality management and the performance of engagements. (Ref: Para. A124–A131A, A134)</p> <p>(f) Appropriate intellectual resources are obtained or developed, implemented and maintained, and appropriately used, to enable the operation of the firm’s system of quality management and the consistent performance of quality engagements, and such intellectual resources are consistent with professional standards and applicable legal and regulatory requirements, where applicable. (Ref: Para. A132–A134)</p> <p>(g) Resources obtained by the firm from service providers, if any, are appropriate for use in the firm’s system of quality management and performance of engagements. (Ref: Para. A134A–A134E)</p>	<p><i>Human Resources</i> (Ref: Para. 38(a)–38(d))</p> <p>A117. Competence is the ability of the individual to perform a role and goes beyond knowledge of principles, standards, concepts, facts, and procedures; it is the integration and application of technical competence, professional skills, and professional ethics, values and attitudes. Competence can be developed through a variety of methods, including professional education, continuing professional development, training, work experience or coaching of less experienced engagement team members by more experienced engagement team members.</p> <p>A118. Professional standards, law or regulation may establish requirements addressing competence and capabilities.</p> <div data-bbox="982 646 1955 881" style="border: 1px solid black; padding: 5px;"> <p><i>Example of requirements in law or regulation that address competence and capabilities</i></p> <p>Law or regulation of a jurisdiction may establish requirements for the professional licensing of engagement partners, including requirements regarding their professional education and continuing professional development.</p> </div> <div data-bbox="909 914 1955 1404" style="border: 1px solid black; padding: 5px;"> <p>A119. <i>Examples of matters that the firm may address regarding hiring, developing and retaining personnel</i></p> <ul style="list-style-type: none"> • The firm may develop a recruitment strategy focused on selecting individuals who have appropriate competency, or the ability to develop it. • The firm’s training programs may focus on developing the competence of personnel. • The firm may address the continuing professional development of personnel, including personnel’s responsibility to maintain an appropriate level of continuing professional development, and how the firm will support them. • The firm may establish evaluation mechanisms that are undertaken at </div>
---	---

	<p>appropriate intervals and include competency areas and other performance measures.</p> <ul style="list-style-type: none">• The firm may set compensation, promotion and other incentives, for all personnel, including engagement partners and individuals assigned roles and responsibilities related to the firm's system of quality management. <p>A120. Individuals assigned to engagements or other roles may include individuals from a a network, another network firm or a service provider, or individuals from a service delivery center. Individuals from a service delivery center may be employed by the firm or they may be employed by a network, another network firm or a service provider. The quality objectives in paragraphs 38(b) and 38(c) apply to all individuals assigned to engagements or other roles in the system of quality management.</p> <p>A121. Timely evaluations and feedback help support and promote the continual development of the competence of personnel. Less formal methods of evaluation and feedback may be used, such as in the case of firms with fewer personnel.</p> <p>A122. Positive actions or behaviors demonstrated by personnel may be recognized through various means, such as through compensation, promotion, or other incentives. In some circumstances, simple or informal incentives that are not based on monetary rewards may be appropriate.</p> <p>A123. The manner in which the firm holds personnel accountable for actions or behaviors that negatively affect quality, such as failing to demonstrate a commitment to quality, develop and maintain the competence to perform their role or implement the firm's responses as designed, may depend on the nature of the action or behavior, including its severity and frequency of occurrence.</p> <p><i>Examples of actions the firm may take when personnel demonstrate actions or behaviors that negatively affect quality</i></p> <ul style="list-style-type: none">• Training or other professional development.• Considering the effect of the matter on the evaluation, compensation, promotion or other incentives of those involved.
--	--

- Disciplinary action, if appropriate.

Technological Resources (Ref: Para. 38(e))

A124. Technological resources, which are typically IT applications, form part of the firm's IT environment. The firm's IT environment also includes the supporting IT infrastructure and the IT processes and human resources involved in those processes:

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

A125. A technological resource may serve multiple purposes within the firm and some of the purposes may be unrelated to the system of quality management. Technological resources that are relevant for the purposes of this ISQM are:

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

Scalability examples to demonstrate how the technological resources that are relevant for the purposes of this ISQM may differ

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

A130. Example of matters that may be considered by the firm in obtaining, developing, implementing and maintaining an IT application

- The data inputs are complete and appropriate.
- Confidentiality of the data is preserved.
- The IT application operates as designed and achieves the purpose for which it is intended.

- The outputs of the IT application achieve the purpose for which they will be used.
- The general IT controls necessary to support the IT application's continued operation as designed are appropriate.
- The need for specialized skills to utilize the IT application effectively, including the training of individuals who will use the IT application.
- The need to develop procedures that set out how the IT application operates.

A131A. The firm may specifically prohibit the use of IT applications or features of IT applications until such time that it has been determined that they operate appropriately and have been approved for use by the firm.

Intellectual Resources (Ref: Para. 38(f))

A132. Intellectual resources include the information the firm uses to promote consistency in the performance of engagements.

Examples of intellectual resources

Written policies or procedures, a methodology, industry or subject matter-specific guides, accounting guides, standardized documentation or access to information sources (e.g., subscriptions to websites that provide in-depth information about entities or other information that is typically used in the performance of engagements).

A133. The intellectual resources may be made available through technological resources.

Example of intellectual resources made available through technological resources

The firm's methodology may be embedded in the IT application that facilitates the planning and performance of the engagement.

Use of Technological and Intellectual Resources (Ref: Para. 38(e)–38(f))

A134. The firm may establish policies or procedures regarding the use of the firm’s technological and intellectual resources. Such policies or procedures may:

- Require the use of certain IT applications or intellectual resources in performing engagements, or relating to other aspects of the engagement, such as in archiving the engagement file.
- Specify the qualifications or experience that individuals need to use the resource, including the need for an expert or training.
- Specify the responsibilities of the engagement partner regarding the use of technological and intellectual resources, including circumstances when technological and intellectual resources are used on the engagement that have been obtained by the engagement team (i.e., the firm has not provided the resource).
- Set out how the technological or intellectual resources are to be used, including how individuals should interact with an IT application or how the intellectual resource should be applied, and the availability of support or assistance in using the technological or intellectual resource.

Example of when qualifications or expertise are needed to use a technological or intellectual resource

The firm may specify the qualifications or expertise needed to use an IT application that analyzes data, given that specialized skills are needed to interpret the results.

Service Providers (Ref: Para. 38(g))

A134A. In some circumstances, the firm may use resources that are provided by a service provider, particularly in circumstances when the firm does not have access to the appropriate resources internally. Service providers are individuals or organizations

external to the firm, who are engaged by the firm and used in the system of quality management, including in the performance of engagements. Service providers exclude networks, network firms or other structures or organizations in the network.

Examples of resources from a service provider

- Individuals engaged to perform the firm's monitoring activities or engagement quality reviews, or to provide consultation on technical matters.
- A commercial IT application used to perform audit engagements.
- Individuals engaged to assist in performing engagements, for example, to attend a physical inventory count or inspect physical fixed assets at a remote location.
- An auditor's external expert engaged by the firm to assist the engagement team in obtaining audit evidence.

A service provider does not include the use of component auditors external to the firm in the context of an audit of group financial statements, or the use of an entity's internal audit function in the performance of engagements, since in both cases they are engaged by the entity.

A134B. The resources provided by service providers are a consideration in identifying and assessing quality risks as part of the firm's risk assessment process.

Examples of characteristics of the service providers used by the firm, and the resources they provide, that the firm may determine give rise to an assessed quality risk

- The resource from the service provider is significant to the firm's system of quality management because it is used extensively across the firm, or it is being used by the firm to address another quality risk.

- The resource from the service provider has been customized by the service provider for the firm.
- The firm has not previously used the service provider and the service provider is not well-known in the market.
- The service provider is new to the industry.

A134C. In determining whether a resource from a service provider is appropriate for use in the firm's system of quality management, the firm may:

- Obtain an understanding of the service provider, including the reputation, competence and capabilities of the service provider;
- Determine the nature and scope of the resources, and the conditions of the service (e.g., in relation to an IT application, how often updates will be provided, limitations on the use of the IT application and how the service provider addresses confidentiality of data).
- Consider how the resource will be used by the firm in its system of quality management and whether it is suitable for that purpose.

A134D. The firm may have responsibilities in using the resources such as the actions the firm needs to take in order to implement the resource or information the firm needs to communicate to the service provider in order that the resource can function effectively (e.g., in relation to an IT application, the firm may need to have supporting IT infrastructure and IT processes in place).

A134E. There may be circumstances when the service provider supplies the firm with an assurance report on the description and design of their controls over the resource, and in some circumstances, it may also include assurance on the operating effectiveness of such controls.

Information and Communication	Information and Communication (Ref: Para. 40)
<p>40. The firm shall establish the following quality objectives that address obtaining, generating or using information regarding the system of quality management, and communicating information within the firm and to external parties on a timely basis to enable the design, implementation and operation of the system of quality management: (Ref: Para. A135)</p> <p>(a) The information system supports the system of quality management by identifying, capturing, processing and maintaining relevant and reliable information, whether from internal or external sources. (Ref: Para. A136–A138A)</p> <p>(b) The culture of the firm promotes and emphasizes the responsibility of individuals to exchange information with the firm and with one another. (Ref: Para. A139)</p> <p>(c) Relevant and reliable information is exchanged throughout the firm, including:</p> <p>(i) Information is communicated to engagement teams and other individuals, the nature, timing and extent of which is sufficient to enable them to understand and carry out their responsibilities relating to the performance of engagements or</p>	<p>A135. Obtaining, generating or communicating information is generally an ongoing process that involves all personnel and encompasses the dissemination of information within the firm and externally. Information and communication is pervasive to all components of the system of quality management.</p> <p><i>The Firm's Information System</i> (Ref: Para. 40(a))</p> <p>A136. Reliable information includes information that is accurate, complete, timely and valid to enable the proper functioning of the firm's system of quality management and to support decisions regarding the system of quality management.</p> <p>A138. The information system may include the use of manual or IT elements, which affect the manner in which information is identified, captured, processed, maintained and communicated. The procedures to identify, capture, process, maintain and communicate information may be enforced through IT applications, and in some cases may be embedded within the firm's responses for other components. In addition, digital records may replace or supplement physical records.</p> <div data-bbox="909 865 1953 1101" style="border: 1px solid black; padding: 5px;"> <p>138A. <i>Scalability example to demonstrate how the information system may be designed in a less complex firm:</i></p> <p>Less complex firms with fewer personnel, and direct involvement of firm leadership may not need rigorous policies and procedures that specify how information should be identified, captured, processed and maintained.</p> </div> <p><i>Communication Within the Firm</i> (Ref: Para. 40(b), 40(c)(i) and 40(c)(ii))</p> <p>A139. The firm may promote and emphasize the responsibility of individuals to exchange information with the firm and with one another by establishing two-way communication channels to facilitate communication across the firm.</p> <div data-bbox="978 1317 1953 1408" style="border: 1px solid black; padding: 5px;"> <p><i>Examples of two-way communication among the firm, engagement teams and other individuals</i></p> </div>

<p>activities within the system of quality management. (Ref: Para. A139)</p> <p>(ii) Personnel communicate relevant and reliable information to the firm when performing engagements or activities within the system of quality management. (Ref: Para. A139)</p> <p>(iii) Information is communicated by the firm to the network or service providers, if any, to enable the network or service providers to fulfill their responsibilities relating to the network requirements or network services or resources provided by the service provider; (Ref: Para. A141A)</p> <p>(iv) Information is communicated by the firm to external parties when required by law, regulation or professional standards, or when the firm determines appropriate to support external parties' understanding of the system of quality management, including the quality of the engagements performed by the firm. (Ref: Para. A142–A153)</p>	<ul style="list-style-type: none"> • The firm communicates the responsibility for implementing the firm's responses to engagement teams and other individuals. • The firm communicates changes to the system of quality management to engagement teams and other individuals, to the extent that the changes are relevant to their responsibilities and enables the engagement teams and other individuals to take prompt and appropriate action in accordance with their responsibilities. • The firm communicates information that is obtained during the firm's acceptance and continuance process that is relevant to engagement teams in planning and performing engagements. • Engagement teams communicate to the firm information about: <ul style="list-style-type: none"> ○ The client that is obtained during the performance of an engagement that may have caused the firm to decline the client relationship or specific engagement had that information been known prior to accepting or continuing the client relationship or specific engagement. ○ The operation of the firm's responses (e.g., concerns about the firm's processes for assigning individuals to engagements), which in some cases, may indicate a finding in the firm's system of quality management. • The individual(s) assigned operational responsibility for compliance with independence requirements communicates to relevant individuals changes in the independence requirements and the firm's policies or procedures to address such changes. • Engagement teams communicate information to the engagement quality reviewer or individuals providing consultation.
--	---

Communication with External Parties

Communication with the Network and Service Providers (Ref: Para. 40(c)(iii))

A141A. In addition to the firm communicating information to the network or a service provider, the firm may need to obtain information from the network or a service provider that supports the firm in the design, implementation and operation of its system of quality management.

Example of a information obtained by the firm from the network

The firm obtains information from the network as therelevant ethical requirements include requirements for independence that apply to network firms or employees of network firms.

Communication Required by Law or Regulation (Ref: Para. 40(c)(iv))

A142. Examples of when law, regulation or professional standards may require the firm to communicate information to external parties

- The firm becomes aware of non-compliance with laws and regulations by a client, and relevant ethical requirements require the firm to report the non-compliance with laws and regulations to an appropriate authority outside the client entity, or to consider whether such reporting is an appropriate action in the circumstances.
- Law, regulation or professional standards require the firm to publish a transparency report and specify the nature of the information that is required to be included in the transparency report.

Communication to External Parties to Support an Understanding of the System of Quality Management (Ref: Para. 40(c)(iv))

A145. 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. In circumstances when the firm is transparent about the activities that it has undertaken to address quality, and the effectiveness of those activities, stakeholders' perception of the quality of engagements performed by the firm may be improved. The form of communication may vary.

Examples of Form of Communication to External Parties

- A webpage.
- A publication such as a transparency report or audit quality report.
- Targeted communication to specific stakeholders (e.g., information about the results of the firm's monitoring and remediation process).
- Direct conversations with the external party.

A146. Examples of matters the firm may consider in determining whether it is appropriate to communicate with external parties to support an understanding of the system of quality management, and the nature, timing and extent of such communication

- The types of engagements performed by the firm, and the types of entities for which such engagements are undertaken and whether there are external parties who may use information about the firm's system of quality management to support their understanding of the quality of the engagements performed by the firm.
- The nature and circumstances of the firm including:
 - The nature of the firm's operating environment, such as customary business practice in the firm's jurisdiction and the characteristics of the financial markets in which the firm operates; and
 - The expectations of stakeholders in the firm's jurisdiction, including the understanding and interest that external parties have expressed about the engagements undertaken by the firm, and the firm's processes in performing the engagements.

- The information that is already available to external parties.
- How external parties may use the information, and their general understanding of matters related to firms' system of quality management and audits or reviews of financial statements, or other assurance or related services engagements.

Examples of external parties who may use information about the firm's system of quality management

- Management or those charged with governance of the firm's clients may use the information to determine whether to appoint the firm to perform an engagement.
- External oversight authorities.
- Other firms who use the work of the firm in the performance of engagements (e.g., in relation to a group audit).
- Other users of the firm's engagement reports for example, investors who use engagement reports in their decision making..

A151. The firm may consider the following attributes in preparing the information that is communicated to external parties about the firm's system of quality management:

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

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

Examples of matters that may be communicated by the firm about its system of quality management

- The nature and circumstances of the firm, such as the organizational structure and operating environment.
- The firm's governance and leadership, such as its culture and commitment to quality and information about the individuals responsible for the leadership of the firm.
- Factors that contribute to quality engagements, for example, such information may be presented in the form of engagement quality indicators with narrative to explain the indicators.
- The results of the firm's monitoring activities and external inspections, and how the firm has remediated identified deficiencies or is otherwise responding to them.
- The evaluation undertaken in accordance with paragraph 65A and 65AA of whether the system of quality management provides the firm with reasonable assurance that the objectives of the system are being achieved, including the basis for the judgments made in undertaking the evaluation.
- How the firm has responded to emerging developments and changes in the circumstances of the firm or its engagements, including how the system of quality management has been adapted to respond to such changes.

	<ul style="list-style-type: none"> The relationship between the firm and the network, the overall structure of the network, a description of network requirements and network services, the responsibilities of the firm and the network, and information about the overall scope and results of network monitoring activities across the network firms. <p>A153. In some cases, law or regulation may preclude the firm from communicating information related to its system of quality management externally.</p> <p><i>Examples of when the firm may be precluded from communicating information externally</i></p> <ul style="list-style-type: none"> Privacy or secrecy law or regulation prohibits disclosure of certain information. Law, regulation or relevant ethical requirements include provisions addressing the duty of confidentiality.
<p>Specified Responses</p>	<p>Specified Responses (Ref: Para. 41A)</p>
<p>41A. In designing and implementing responses, the firm shall include the following responses in accordance with paragraph 22F: (Ref: Para. A153A)</p> <p>(a) The firm assigns operational responsibility for compliance with independence requirements to an individual(s) who fulfills the criteria in paragraph 22AA. (Ref: Para. A153B)</p> <p>(b) The firm obtains, at least annually, a documented confirmation of compliance with independence requirements from all personnel required by relevant ethical requirements to be independent.</p>	<p>A153A. The specified responses alone are not sufficient to achieve the objectives of the system of quality management and may address quality risks that are relevant to multiple components.</p> <p><i>Responsibility for Compliance with Independence Requirements</i> (Ref: Para. 41A(a))</p> <p>A153B. Compliance with independence requirements is essential to the performance of audits, or reviews of financial statements, or other assurance engagements, and is an expectation of stakeholders relying on the firm's reports. The individual assigned operational responsibility for compliance with independence requirements is ordinarily responsible for the oversight of all matters related to independence so that a robust and consistent approach is designed and implemented by the firm to deal with independence requirements.</p>

<p>(c) The firm establishes policies or procedures for receiving, investigating and resolving complaints and allegations about the commitment to quality of the firm or its personnel. (Ref: Para. A153C–A153D)</p> <p>(d) The firm establishes policies or procedures to address circumstances when:</p> <p>(i) The firm becomes aware of information subsequent to accepting or continuing a client relationship or specific engagement that would have caused it to decline the client relationship or specific engagement had that information been known prior to accepting or continuing the client relationship or specific engagement; or (Ref: Para. A153E–A153G)</p> <p>(ii) The firm is obligated by law or regulation to accept a client relationship or specific engagement. (Ref: Para. A153F–A153G)</p> <p>(e) [Placeholder for engagement quality reviews – refer to Agenda Item 5]</p>	<p><i>Complaints and Allegations</i> (Ref: Para. 41A(c))</p> <p>A153C. Establishing policies or procedures for dealing with complaints and allegations about a failure to perform work in accordance with professional standards and applicable legal and regulatory requirements, or non-compliance with the firm’s policies or procedures, may assist the firm in preventing engagement reports from being issued that are inappropriate. It also may assist the firm in:</p> <ul style="list-style-type: none"> • Identifying and dealing with individual(s), including leadership, who do not act or behave in a manner that supports the firm’s commitment to quality; or • Identifying findings in the system of quality management. <p>A153D. Complaints and allegations may originate from within or outside the firm and they may be made by individuals internal or external to the firm (e.g., clients or others within the firm’s network).</p> <p><i>Information That Becomes Known Subsequent to Accepting or Continuing a Client Relationship or Specific Engagement</i> (Ref: Para. 41A(d))</p> <p>A153E. Information that becomes known subsequent to accepting or continuing a client relationship or specific engagement may:</p> <ul style="list-style-type: none"> • Have existed at the time of the firm’s decision to accept or continue the client relationship or specific engagement and the firm was not aware of such information; or • Relate to new information that has arisen since the decision to accept or continue the client relationship or specific engagement. <div style="border: 1px solid black; padding: 5px; margin-top: 10px;"> <p><i>Examples of matters addressed in the firm’s policies or procedures for circumstances when information becomes known subsequent to accepting or continuing a client relationship or specific engagement that may have affected the firm’s decision to accept or continue a client relationship or specific engagement</i></p> <ul style="list-style-type: none"> • Undertaking consultation within the firm or with legal counsel. </div>
---	---

- Considering whether there is a professional, legal or regulatory requirement for the firm to continue the engagement.
- Discussing with the appropriate level of the client's management and with those charged with governance or the engaging party the action that the firm might take based on the relevant facts and circumstances, and when it is determined that withdrawal is an appropriate action, informing them of this decision and the reasons for the withdrawal.
- If the firm withdraws from the engagement, considering whether there is a professional, legal or regulatory requirement for the firm to report the withdrawal from the engagement, or from both the engagement and the client relationship, together with the reasons for the withdrawal, to regulatory authorities.

A153F. In some circumstances, jurisdictional law or regulation may impose an obligation on the firm to accept or continue a client engagement, or in the case of the public sector, the firm may be appointed through statutory provisions.

A153G. Example of matters addressed in the firm's policies or procedures in circumstances when the firm is aware of information that would have caused the firm to decline or discontinue an engagement, however the firm is obligated to accept or continue the engagement or the firm is unable to withdraw from the engagement

- The firm considers the effect of the information obtained in determining whether to accept or continue a client relationship or specific engagement on the performance of the engagement.
- The firm communicates the information to the engagement partner, and requests the engagement partner to increase the extent and frequency of their direction and supervision of engagement team members and review of their work.
- The firm assigns more experienced individuals to the engagement.

	<ul style="list-style-type: none"> • The firm determines that an engagement quality review should be performed. <p><i>Engagements Subject to an Engagement Quality Review</i> (Ref: Para. 41A(e)) [Placeholder for application material– refer to Agenda Item 5]</p>
<p>Monitoring and Remediation Process</p> <p>42. The firm shall establish a monitoring and remediation process to: (Ref: Para. A154)</p> <p>(a) Provide relevant, reliable and timely information about the design, implementation and operation of the system of quality management.</p> <p>(b) Take appropriate actions to respond to identified deficiencies such that deficiencies are remediated on a timely basis.</p>	<p>Monitoring and Remediation Process (Ref: Para. 42–54)</p> <p>A154. In addition to enabling the firm’s evaluation of the system of quality management, the monitoring and remediation process facilitates the proactive and continual improvement of engagement quality and the system of quality management.</p>
<p>43A. The firm shall assign operational responsibility for the monitoring and remediation process to an individual(s) who fulfills the criteria in paragraph 22AA.</p>	
<p><i>Designing and Performing Monitoring Activities</i></p> <p>44. The firm shall design and perform monitoring activities to prevent or detect deficiencies that, individually or in aggregate, could result in the system of quality management not providing the firm with reasonable assurance that the objectives of the system are being achieved. In determining the nature, timing and extent of the monitoring activities,</p>	<p><i>Designing and Performing Monitoring Activities</i> (Ref: Para. 44–46)</p> <p>A155A. The monitoring activities undertaken by the firm may detect a deficiency, or may prevent a deficiency from arising through responding to a finding before it rises to a level of severity or pervasiveness that results in a deficiency.</p> <p>A156. In most cases, ongoing monitoring activities identify findings in the system of quality management in a timelier manner.</p>

<p>including the appropriate combination of ongoing and periodic monitoring activities, the firm shall take into account: (Ref: Para. A155A–A159)</p> <p>(a) The reasons for the assessments given to the quality risks, including:</p> <p>(i) The factors giving rise to the quality risks; and (Ref: Para. A159B)</p> <p>(ii) The likelihood of the quality risks occurring and the effect of the quality risks on the achievement of a quality objective(s);</p> <p>(b) The design of the responses;</p> <p>(c) For monitoring activities over the firm’s risk assessment process, the design of that process; (Ref: Para. A161A)</p> <p>(d) Changes in the system of quality management. (Ref: Para. A162)</p> <p>(e) The results of previous monitoring activities, whether previous monitoring activities continue to be relevant in evaluating the firm’s system of quality management and whether remedial actions to address previously identified deficiencies were effective; and (Ref: Para. A163–A164)</p> <p>(f) Other relevant information, including concerns identified regarding the commitment to quality of the firm or its personnel and information from external inspections. (Ref: Para. A165–A167)</p>	<p>A157. Monitoring activities may include the inspection of in-process engagements. Inspections of engagements are designed to monitor that an aspect of the system of quality management is designed, implemented and operating in the manner intended. In some circumstances, the system of quality management may include responses that are designed to review engagements while in process that appear similar in nature to an inspection of in-process engagements (e.g., reviews that are designed to detect failures or shortcomings in the system of quality management so that they can prevent an assessed quality risk from occurring). The purpose of the activity will guide its design and implementation, and where it fits within the system of quality management (i.e., whether it is a monitoring activity that is an inspection of in-process engagement or an engagement review that is a response to address an assessed quality risk).</p> <p>A158. The nature, timing and extent of the monitoring activities may also be affected by other matters, including:</p> <ul style="list-style-type: none"> • The size, structure and organization of the firm. • The involvement of the network in monitoring activities. • The resources that the firm intends to use to enable monitoring activities, such as the use of IT applications. <p>A159. When performing monitoring activities, the firm may determine that changes to the nature, timing and extent of the monitoring activities are needed, such as when findings indicate the need for more extensive monitoring activities.</p> <p>The Reasons for the Assessments Given to the Quality Risks (Ref: Para. 44(a))</p> <p>A159B. The factors giving rise to the quality risks include the nature and circumstances of the firm and the engagements it performs, as set out in paragraph 22E of this ISQM.</p> <p>The Design of the Firm’s Risk Assessment Process (Ref: Para. 44(c))</p>
---	---

A161A. How the firm's risk assessment process is designed (e.g., a centralized or decentralized process, or the frequency of review) may affect the nature, timing and extent of the monitoring activities.

Changes in the System of Quality Management (Ref: Para. 44(d))

A162. Changes in the system of quality management may include:

- Changes to address an identified deficiency in the system of quality management.
- Changes to the responses.

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

Examples of matters that may give rise to change to the responses

- Changes in the nature and circumstances of the firm and the engagements it performs.
- Responses have become obsolete over time.
- More effective responses are available, such as the use of IT applications to replace manual processes.

Previous Monitoring Activities (Ref: Para. 44(e), 50)

A163. The results of the firm's previous monitoring activities may indicate areas of the system where a deficiency may arise, particularly areas where there is a history of deficiencies. Furthermore, the monitoring activities may need to evaluate the effectiveness of the remedial actions that have been implemented to address deficiencies previously identified.

	<p>A164. Previous monitoring activities undertaken by the firm on areas of the system of quality management that have not changed may no longer provide the firm with information to support the evaluation of the system, including in circumstances when time has elapsed since the monitoring activities were undertaken.</p> <p>Other Relevant Information (Ref: Para. 44(f))</p> <p>A165. In addition to the sources of information indicated in paragraph 44(f), other relevant information may include:</p> <ul style="list-style-type: none"> • Information communicated by the network in accordance with paragraphs 60(c) and 61(b) about the firm’s system of quality management, including the network requirements or network services that the firm has included in its system of quality management. • Information communicated by a service provider about the resources the firm uses in its system of quality management. • Information available from other regulators, such as information from a securities regulator about an entity for whom the firm performs engagements (e.g., irregularities in their financial statements). <p>A166. The results of external inspections or other relevant information, both internal and external, may indicate that previous monitoring activities undertaken by the firm failed to identify a deficiency in the system of quality management. This information may affect the firm’s consideration of the nature, timing and extent of the monitoring activities.</p> <p>A167. External inspections are not a substitute for the firm’s internal monitoring activities. Nevertheless, the results of external inspections may provide a basis for the nature, timing and extent of the monitoring activities.</p>
<p>45. The firm shall include the inspection of completed engagements in its monitoring activities. In determining the selection of engagements for inspection, and taking into account the matters in</p>	<p><i>Engagement Inspections</i> (Ref: Para. 45)</p> <p>A168. The matters in paragraph A158 may also affect the firm’s selection of completed engagements for inspection.</p>

<p>paragraph 44, the firm shall: (Ref: Para. A168–A170)</p> <p>(a) Consider the nature, timing and extent of other monitoring activities undertaken by the firm and the engagements and engagement partners subject to such monitoring activities; and</p> <p>(b) Select at least one completed engagement for each engagement partner on a cyclical basis determined by the firm.</p>	<p><i>Examples of matters in paragraph 44 that may be considered by the firm in selecting completed engagements for inspection</i></p> <ul style="list-style-type: none"> • In relation to the factors giving rise to the quality risks: <ul style="list-style-type: none"> ○ The types of engagements performed by the firm, and the extent of the firm’s experience in performing the type of engagement. ○ The types of entities for which engagements are undertaken, for example: <ul style="list-style-type: none"> • Entities that are listed, • Entities operating in emerging industries. • Entities operating in industries associated with a high level of complexity or judgment. • Entities operating in an industry that is new to the firm. ○ The tenure and experience of engagement partners. • The results of previous inspections of completed engagements, including for each engagement partner. • In relation to other relevant information: <ul style="list-style-type: none"> ○ Complaints or allegations regarding an engagement partner’s commitment to quality. ○ The results of external inspections, including for each engagement partner. ○ The results of the firm’s evaluation of each engagement partner’s commitment to quality. <p><i>A168B.Examples of how the the nature, timing and extent of other monitoring activities undertaken by the firm and the engagements and engagement</i></p>
--	--

partners subject to such monitoring activities may affect the inspection of completed engagements

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

- Which completed engagements should be selected for inspection.
- Which engagement partners should be selected for inspection, and which engagements that the partner is responsible for should be selected.
- How frequently an engagement partner should be selected for inspection.
- The matters to be considered when performing the inspection of completed engagements.

A169. The inspection of completed engagements for engagement partners on a cyclical basis may assist the firm in monitoring whether engagement partners have fulfilled their overall responsibility for managing and achieving quality on the engagements they are assigned to.

A169A. Examples of how the firm may apply a cyclical basis for the inspection of completed engagements for each engagement partner

The firm may establish policies or procedures that require the inspection of a completed engagement for each engagement partner performing audits of financial statements of listed entities once every three years. The firm's policies or procedures may also include the selection of:

- Engagement partners in a manner that is unpredictable; and
- Engagements or engagement partners where there is an increased need to do so.

The firm's policies or procedures therefore:

- Address the selection of engagement partners more frequently than three years if certain conditions or circumstances exist, such as when:
 - The engagement partner performs an engagement for an entity that has a higher public interest or public accountability, or high public profile, and the engagement has not been subject to a completed inspection in the last three years;
 - The engagement partner performs engagements for entities operating in a certain industry where there are increased risks of audit failures.
 - An engagement performed by the engagement partner has been subject to other monitoring activities, and the results of the other monitoring activities were unsatisfactory.
 - The engagement partner has performed an engagement for an entity operating in an industry in which the engagement partner has limited experience.
 - The engagement partner is a newly appointed engagement partner, or has recently joined the firm from another firm or another jurisdiction.
- Allow the selection of the engagement partner to be deferred for a period(s) if certain conditions or circumstances exist, such as when engagements performed by the engagement partner have been subject to other monitoring activities, and the results of the other monitoring activities provide sufficient information about the engagement partner, i.e., performing the inspection of completed engagements would unlikely provide the firm with any further information about the engagement partner.

A170. The matters considered in an inspection of an engagement depends on how the inspection will be used to monitor the system of quality management. Ordinarily, the

	<p>inspection of an engagement includes determining that responses designed to be implemented at the engagement level have been implemented.</p> <div style="border: 1px solid black; padding: 5px;"> <p><i>Example of a response at the engagement level that is considered by the firm in an inspection of an engagement</i> In inspecting engagements, the firm determines whether engagement teams have appropriately applied a change in the firm's methodology arising from changes in professional standards.</p> </div>
<p>46. The firm shall establish policies or procedures that:</p> <p>(a) Require the individuals performing the monitoring activities to have the competence and capabilities, including sufficient time, to perform the monitoring activities effectively; and</p> <p>(b) Address the objectivity of the individuals performing the monitoring activities. Such policies or procedures shall prohibit the engagement team members or the engagement quality reviewer of an engagement from performing any inspection of that engagement. (Ref: Para. A171)</p>	<p>Individuals Performing the Monitoring Activities (Ref: Para. 46(b))</p> <p>A171. The provisions of relevant ethical requirements are relevant in designing the policies or procedures addressing the objectivity of the individuals performing the monitoring activities. A self-review threat may arise when an individual who performs:</p> <ul style="list-style-type: none"> • An inspection of an engagement was: <ul style="list-style-type: none"> ○ In the case of an audit of financial statements, an engagement team member or the engagement quality reviewer of that engagement or an engagement for a subsequent financial period; or ○ For all other engagements, an engagement team member or the engagement quality reviewer of that engagement. • Another type of monitoring activity had participated in designing, executing or operating the response being monitored.
<p><i>Evaluating Findings and Identifying Deficiencies</i></p> <p>47. The firm shall establish policies or procedures addressing the evaluation of the findings to determine whether deficiencies exist, including in the monitoring and remediation process. (Ref: Para. A173–A177)</p>	<p><i>Evaluating Findings and Identifying Deficiencies</i> (Ref: Para. 47)</p> <p>A173. The results of monitoring activities, results of external inspections and other relevant information may reveal other observations about the firm's system of quality management, such as:</p> <ul style="list-style-type: none"> • Actions, behaviors or conditions that have given rise to positive outcomes in the context of quality or the effectiveness of the system of quality management; or

- When findings are identified, observations that similar findings did not arise in other circumstances that are of a similar nature to the matter to which the finding relates (e.g., in relation to engagements, observations that findings were not observed on other engagements of a similar nature).

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

A173A. The firm may exercise professional judgment in determining whether a finding, individually or in combination with other findings, is of such significance that it results in a deficiency in the system of quality management. Significance is judged by the firm, taking into consideration the relative importance of the finding in the context of the aspect of the system of quality management to which it relates. The firm's judgments may be affected by quantitative and qualitative factors relevant to the finding. In some circumstances, the firm may determine it appropriate to investigate the root cause(s) of a finding in order to determine whether a finding is a deficiency.

A173B. Not all findings, including engagement findings, will be a deficiency in the system of quality management.

A175. Examples of quantitative and qualitative factors that a firm may consider in determining whether a finding(s) is of such significance that it results in a deficiency

Quality risks and responses

- If the finding relates to a response:
 - The design of the response.
 - The nature of the assessed quality risk to which the response relates, and the extent to which the finding indicates that the assessed quality risk has not been addressed.

- Whether there are other responses that address the same assessed quality risk and whether there are findings for those responses.

Nature of the finding and its pervasiveness

- The nature of the finding. For example, a finding related to leadership's actions and behaviors may be qualitatively significant, given the pervasive effect this may have on the system of quality management as a whole.
- Whether the finding, in combination with other findings, indicates a trend or systemic issue. For example, similar engagement findings that appear on multiple engagements may indicate a systemic issue.

Error rates and population size

- The design of the monitoring activity from which the finding arose. For example, the firm may consider the tolerable error rate of the activity and whether it was designed to focus on specific areas of risk or the whole population.
- The extent of the monitoring activity from which the finding arose, including the size of sample selected relative to the size of the entire population.
- The extent of the findings in relation to the sample of the population covered by the monitoring activity. For example, in the case of inspection of engagements, the number of engagements selected where the finding was identified, relative to the total number of engagements selected.

A175A. Evaluating findings and identifying deficiencies, evaluating the severity and pervasiveness of a deficiency and investigating the root cause(s) of a deficiency are iterative.

	<p><i>Examples of the iterative nature of evaluating findings and identifying deficiencies, evaluating identified deficiencies, and investigating the root cause(s) of deficiencies</i></p> <ul style="list-style-type: none"> • In investigating the root cause(s) of a deficiency, the firm identifies a circumstance that also existed in relation to another finding that is not considered a deficiency. As a result, the firm adjusts its evaluation of the other finding and classifies it as a deficiency. • In evaluating the severity and pervasiveness of a deficiency, the firm identifies a trend or systemic issue that correlates with other findings that are not considered deficiencies. As a result, the firm adjusts its evaluation of the other findings and also classifies them as deficiencies. <p>A177. The results of monitoring activities, results of external inspections and other relevant information (e.g., network monitoring activities or complaints and allegations) may reveal information about the effectiveness of the monitoring and remediation process.</p> <p><i>Example of how external inspection findings may reveal information about the effectiveness of the monitoring and remediation process</i></p> <p>External inspection findings may indicate findings in the system of quality management that have not been identified by the firm’s monitoring and remediation process, which may highlight a deficiency in that process.</p>
<p><i>Evaluating Identified Deficiencies</i></p> <p>48. The firm shall establish policies or procedures addressing: (Ref: Para. A175A)</p> <p>(a) The investigation of the root cause(s) of the identified deficiencies, including that the nature, timing and extent of the procedures to be performed to investigate the root cause(s)</p>	<p><i>Root Cause of the Identified Deficiencies</i> (Ref: Para. 48(a))</p> <p>A179. The objective of investigating the root cause(s) of identified deficiencies is to understand the underlying circumstances that caused the deficiencies to enable the firm to:</p> <ul style="list-style-type: none"> • Evaluate the severity and pervasiveness of the deficiency; and • Appropriately remediate the deficiency.

<p>take into account the nature of the identified deficiencies and their possible severity; and (Ref: Para. A179–A182A)</p> <p>(b) The evaluation of the severity and pervasiveness of the identified deficiencies, including the effect of the identified deficiencies, individually and in aggregate, on the system of quality management. (Ref: Para. A183–A183A)</p>	<p>Performing a root cause analysis involves those performing the assessment exercising professional judgment based on the evidence available.</p> <p>A180. The nature and circumstances of the firm, such as the complexity and operating characteristics of the firm, the size of the firm, the geographical dispersion of the firm, how the firm is structured or the extent to which the firm concentrates or centralizes its processes or activities, may also affect the nature, timing and extent of the procedures undertaken to understand the root cause(s) of an identified deficiency.</p> <div data-bbox="982 537 1948 1380" style="border: 1px solid black; padding: 10px;"><p><i>Examples of how the nature of identified deficiencies and their possible severity and the nature and circumstances of the firm may affect the nature, timing and extent of the procedures undertaken to understand the root cause(s) of the identified deficiencies</i></p><ul style="list-style-type: none">• The nature of the identified deficiency: The firm’s procedures to understand the root cause(s) of an identified deficiency may be more rigorous in circumstances when an engagement report related to an audit of financial statements of a listed entity was issued that was inappropriate or the identified deficiency relates to leadership’s actions and behaviors regarding quality.• The possible severity of the deficiency: The firm’s procedures to understand the root cause(s) of an identified deficiency may be more rigorous in circumstances when the deficiency has been identified across multiple engagements or there is an indication that policies or procedures have high rates of non-compliance.• Nature and circumstances of the firm: In the case of a less complex firm with a single location, the firm’s procedures to understand the root cause(s) of a deficiency may be simple, since the information to inform the understanding may be readily available and concentrated, and the root cause(s) may be more apparent. However, in the case of a more complex firm with multiple locations, the procedures to understand the root cause(s)</div>
--	---

of a deficiency may include using individuals specifically trained on investigating the root cause(s) of identified deficiencies, and developing a methodology with more formalized procedures for identifying root cause(s).

A181A. In investigating the root cause(s) of identified deficiencies, the firm may consider why deficiencies did not arise in other circumstances that are of a similar nature to the matter to which the deficiency relates. Such information may also be useful in determining how to remediate an identified deficiency.

Example of when a deficiency did not arise in other circumstances of a similar nature, and how this information assists the firm in investigating the root cause(s) of identified deficiencies

The firm identifies findings on multiple engagements that are audits of financial statements and determines that a deficiency in the system of quality management exists since the finding has occurred across multiple engagements. However, the firm observes several other engagements without these findings, and in considering why these other engagements do not have similar findings, the firm notes that the engagement partners were actively involved at all stages of the engagements. In contrast, for the engagements with the findings, the engagement partners were not actively involved. By contrasting the engagements, the firm concludes that the root cause of the deficiency is a lack of appropriate involvement by the engagement partners at key stages of the engagement.

A182. Identifying a root cause(s) that is appropriately specific may support the firm's process for remediating identified deficiencies.

Example of identifying a root cause(s) that is appropriately specific

The firm identifies that engagement teams performing audits of financial statements are failing to obtain sufficient appropriate audit evidence on accounting estimates where management's assumptions have a high degree of subjectivity. While the firm notes that engagement teams are not exercising appropriate professional skepticism, the underlying root cause of this issue may

relate to another matter, such as a cultural environment that does not encourage engagement team members to challenge individuals with greater authority or insufficient direction, supervision and review of the work performed on the engagements.

A182A. Although not required by this ISQM, investigating the root cause of positive outcomes may reveal opportunities for the firm to improve, or further enhance, the system of quality management.

Evaluating the Severity and Pervasiveness of Identified Deficiencies (Ref: Para. 48(b))

A183. Factors the firm may consider in evaluating the severity and pervasiveness of an identified deficiency include:

- The nature of the identified deficiency, including the aspect of the firm's system of quality management to which the deficiency relates, and whether the deficiency is in the design, implementation or operation of the system of quality management;
- In the case of deficiencies related to responses, whether there are compensating responses to address the assessed quality risk to which the response relates;
- The root cause(s) of the identified deficiency;
- The frequency with which the underlying finding occurred; and
- The magnitude of the identified deficiency, how quickly it occurred and the duration of time that it existed and had an effect on the system of quality management.

A183A. The severity and pervasiveness of deficiencies affects the evaluation of the system of quality management that is undertaken by the individual(s) assigned ultimate responsibility and accountability for the system of quality management.

<p><i>Responding to Identified Deficiencies</i></p> <p>49. The firm shall design and implement remedial actions to address identified deficiencies that are responsive to the results of the root cause analysis. (Ref: Para. A184–A184B)</p>	<p><i>Responding to Identified Deficiencies</i> (Ref: Para. 49)</p> <p>A184. The nature, timing and extent of remedial actions may depend on a variety of other factors, including:</p> <ul style="list-style-type: none"> • The root cause(s). • The severity and pervasiveness of the identified deficiency and therefore the urgency in which it needs to be addressed. • The effectiveness of the remedial actions in addressing the root cause(s), such as whether the firm needs to implement more than one remedial action in order to effectively address the root cause(s), or needs to implement remedial actions as interim measures until the firm is able to implement more effective remedial actions. <p>A184A. In some circumstances, the remedial action may include establishing additional quality objectives, or modifying the assessed quality risks or responses, because it is determined that they are not appropriate.</p> <p>A184B. In circumstances when the firm determines that the root cause of an identified deficiency relates to a resource provided by a service provider, the remedial actions taken by the firm may include:</p> <ul style="list-style-type: none"> • Considering whether to continue using the resources provided by the service provider. • Determining the remedial actions the firm needs to take to address the effect of the identified deficiency. • Communicating the matter to the service provider.
<p>50. The individual(s) assigned operational responsibility for monitoring and remediation shall evaluate whether the remedial actions:</p> <p>(a) Are appropriately designed to address the identified deficiencies and their related root</p>	

<p>cause(s) and determine that they have been implemented; and</p> <p>(b) Implemented to address previously identified deficiencies are effective. (Ref: Para. A163)</p> <p>If the evaluation indicates that the remedial actions are not appropriately designed and implemented or are not effective, the individual(s) assigned operational responsibility for monitoring and remediation shall take appropriate action to modify the remedial actions such that they are effective.</p>	
<p>Findings About a Particular Engagement</p> <p>51. The firm shall respond to circumstances when findings indicate that there is an engagement(s) for which procedures required were omitted during the performance of the engagement(s) or the report issued may be inappropriate. The firm's response shall include: (Ref: Para. A185)</p> <p>(a) Taking appropriate action to comply with relevant professional standards and applicable legal and regulatory requirements; and</p> <p>(b) When the report is considered to be inappropriate, considering the implications and taking appropriate action, including considering whether to obtain legal advice.</p>	<p>Findings About a Particular Engagement (Ref: Para. 51)</p> <p>A185. In circumstances when procedures were omitted or the report issued is inappropriate, the action taken by the firm may include:</p> <ul style="list-style-type: none"> • Consulting with appropriate personnel regarding the appropriate action. • Discussing the matter with management of the entity or those charged with governance. • Performing the omitted procedures. <p>The actions taken by the firm do not relieve the firm of the responsibility to take further actions relating to the finding in the context of the system of quality management, including evaluating the findings, identifying deficiencies and if it is determined that a deficiency exists, investigating the root cause(s) of the identified deficiency.</p>

<p><i>Ongoing Communication Related to Monitoring and Remediation</i></p> <p>52. The individual(s) assigned operational responsibility for the monitoring and remediation process shall communicate on a timely basis to the individual(s) assigned ultimate responsibility and accountability for the system of quality management and the individual(s) assigned operational responsibility for the system of quality management: (Ref: Para. A186)</p> <ul style="list-style-type: none"> (a) A description of the monitoring activities performed; (b) The identified deficiencies, including the severity and pervasiveness of such deficiencies; and (c) The remedial actions to address the identified deficiencies. 	<p><i>Ongoing Communication Related to the Monitoring and Remediation (Ref: Para. 52)</i></p> <p>A186. The information communicated about the monitoring and remediation to the individual(s) assigned ultimate responsibility and accountability for the system of quality management provides the basis for the evaluation of the system of quality management, as required by paragraph 65A.</p>
<p>53. The firm shall communicate the matters described in paragraph 52 to engagement teams and other individuals to enable them to take prompt and appropriate action in accordance with their responsibilities.</p>	
<p>54. The firm shall communicate information about the results of the firm's monitoring and remediation process to external parties on a timely basis, in accordance with paragraph 40(c)(iv).</p>	

Network Requirements or Network Services	Network Requirements or Network Services (Ref: Para. 58)
<p>58. When the firm operates as part of a network, the firm shall understand, when applicable: (Ref: Para. A192)</p> <p>(a) The requirements established by the network regarding the firm’s system of quality management, including requirements for the firm to implement or use resources or services designed or otherwise provided by or through the network (i.e., network requirements);</p> <p>(b) Any services or resources provided by the network that the firm chooses to implement or use in the design, implementation or operation of the firm’s system of quality management (i.e., network services); and</p> <p>(c) The firm’s responsibilities for any actions that are necessary to implement the network requirements or use network services. (Ref: Para. A194)</p> <p>The firm remains responsible for its system of quality management, including professional judgments made in the design, implementation and operation of the system of quality management. The firm shall not allow compliance with the network requirements or use of network services to contravene the requirements of this ISQM. (Ref: Para. A13, A195)</p>	<p>A192. In some circumstances, the firm may belong to a network. Networks may establish requirements regarding the firm’s system of quality management or may make services or resources available that the firm may choose to implement or use in the design, implementation and operation of its system of quality management. Such requirements or services may be intended to promote the consistent performance of quality engagements across the firms that operate as part of the network. The extent to which a network will provide the firm with quality objectives, quality risks and responses that are common across the network will depend on the firm’s arrangements with the network.</p> <div data-bbox="982 630 1953 1255" style="border: 1px solid black; padding: 10px;"> <p><i>Examples of network requirements</i></p> <ul style="list-style-type: none"> • Requirements for the firm to include additional quality objectives or identified quality risks in the firm’s system of quality management that are common across the network firms. • Requirements for the firm to include responses in the firm’s system of quality management that are common across the network firms. Such responses designed by the network may include network policies or procedures that specify the leadership roles and responsibilities, including how the firm is expected to assign authority and responsibility within the firm or resources, such as network developed methodologies for the performance of engagements or IT applications. • Requirements that the firm be subject to the network’s monitoring activities. These monitoring activities may relate to network requirements (e.g., monitoring that the firm has implemented the network’s methodology appropriately), or to the firm’s system of quality management in general. </div>

	<p><i>Examples of network services</i></p> <ul style="list-style-type: none">• Services or resources that are optional for the firm to use as a response in its system of quality management, such as voluntary training programs, or a service delivery center established at the network level, or by another firm or group of firms within the same network. <p>A194. The network may establish responsibilities for the firm in implementing the network requirements or network services.</p> <p><i>Example of responsibilities for the firm in implementing network requirements or network services</i></p> <p>The firm is required to have certain IT infrastructure and IT processes in place to support an IT application provided by the network that the firm uses in the system of quality management.</p> <p>A195. The firm's understanding of the network requirements or network services and the firm's responsibilities relating to the implementation thereof may be obtained through inquiries of, or documentation provided by, the network about matters such as:</p> <ul style="list-style-type: none">• The network's governance and leadership.• The procedures undertaken by the network in designing, implementing and, if applicable, operating, the network requirements or network services.• How the network identifies and responds to changes that affect the network requirements or network services or other information, such as changes in the professional standards or information that indicates a deficiency in the network requirements or network services.• How the network monitors the appropriateness of the network requirements or network services, which may include through the network firms' monitoring activities, and the network's processes for remediating identified deficiencies.
--	--

<p>59. Based on the understanding, the firm shall:</p> <p>(a) Determine how the network requirements or network services are relevant to, and are taken into account in, the firm’s system of quality management, including how they are to be implemented; and (Ref: Para. A196)</p> <p>(b) Evaluate whether and if so, how the network requirements or network services need to be adapted or supplemented by the firm to be appropriate for use in its system of quality management. (Ref: Para. A197)</p>	<p><i>Network Requirements or Network Services in the Firm’s System of Quality Management</i> (Ref: Para. 59)</p> <p>A196. The characteristics of the network requirements or network services are a factor in identifying and assessing quality risks as part of the firm’s risk assessment process.</p> <div data-bbox="982 370 1953 669" style="border: 1px solid black; padding: 5px;"> <p><i>Example of a network requirement or network service that gives rise to a quality risk</i></p> <p>A network requires the firm to use an IT application for the acceptance and continuance of client relationships and specific engagements that is standardized across the network. This gives rise to a quality risk that the IT application does not address matters in local law or regulation that need to be considered by the firm in accepting and continuing client relationships and specific engagements.</p> </div> <p>A197. The purpose of the network requirements may include the promotion of consistent performance of quality engagements across the firms that operate as part of the network. The firm may be expected by the network to implement the network requirements, however, the firm may need to adapt or supplement the network requirements such that they are appropriate for the nature and circumstances of the firm and the engagements it performs.</p> <div data-bbox="982 925 1953 1388" style="border: 1px solid black; padding: 5px;"> <p><i>Examples of how the network requirements or networks services may need to be adapted or supplemented</i></p> <table border="1" data-bbox="982 1019 1953 1388"> <thead> <tr> <th data-bbox="982 1019 1453 1114">Network requirement or network service</th> <th data-bbox="1453 1019 1953 1114">How the firm adapts or supplements the network requirement or network service</th> </tr> </thead> <tbody> <tr> <td data-bbox="982 1114 1453 1388"> The network requires the firm to include certain quality risks in the system of quality management, so that all firms in the network address the quality risks. The network does not provide an assessment of the quality risks. </td> <td data-bbox="1453 1114 1953 1388"> As part of identifying and assessing quality risks, the firm assesses the quality risks that are required by the network. The firm also designs and implements responses to address the assessed risks. </td> </tr> </tbody> </table> </div>	Network requirement or network service	How the firm adapts or supplements the network requirement or network service	The network requires the firm to include certain quality risks in the system of quality management, so that all firms in the network address the quality risks. The network does not provide an assessment of the quality risks.	As part of identifying and assessing quality risks, the firm assesses the quality risks that are required by the network. The firm also designs and implements responses to address the assessed risks.
Network requirement or network service	How the firm adapts or supplements the network requirement or network service				
The network requires the firm to include certain quality risks in the system of quality management, so that all firms in the network address the quality risks. The network does not provide an assessment of the quality risks.	As part of identifying and assessing quality risks, the firm assesses the quality risks that are required by the network. The firm also designs and implements responses to address the assessed risks.				

			<p>quality risks that are required by the network.</p>
		<p>The network requires that the firm design and implement certain responses.</p>	<p>As part of designing and implementing responses, the firm determines:</p> <ul style="list-style-type: none"> • How the responses required by the network will be incorporated into the firm’s system of quality management, given the nature and circumstances of the firm. This may include tailoring the response to reflect the nature and circumstances of the firm and the engagements performed by the firm (e.g., tailoring a methodology to include matters related to law or regulation). • Which assessed quality risks the responses address.
<p><i>Monitoring Activities Undertaken by the Network on the Firm’s System of Quality Management</i></p> <p>60. In circumstances when the network performs monitoring activities relating to the firm’s system of quality management, the firm shall:</p> <p>(a) Determine the effect of the monitoring activities performed by the network on the nature, timing and extent of the firm’s monitoring activities performed in accordance with paragraphs 44–45; (Ref: Para. A199)</p>	<p><i>Monitoring Activities Undertaken by the Network on the Firm’s System of Quality Management (Ref: Para. 60)</i></p> <p>A199. The monitoring activities undertaken by the network may affect the nature, timing and extent of the firm’s monitoring activities.</p> <div style="border: 1px solid black; padding: 5px; margin-top: 10px;"> <p><i>Example of how monitoring activities undertaken by the network affect the firm’s monitoring activities</i></p> <p>The network undertakes inspections of completed engagements of the firm. The firm determines, in the context of the scope and results of the network’s inspection of the firm’s engagements, the extent of engagements that will be selected by the firm in inspecting completed engagements.</p> </div>		

<p>(b) Determine the firm’s responsibilities in relation to the monitoring activities, including any related actions by the firm; and</p> <p>(c) As part of evaluating findings and identifying deficiencies in paragraph 47, obtain the results of the monitoring activities from the network in a timely manner. (Ref: Para. A200)</p>	<p>A200. The results of the network’s monitoring activities of the firm’s system of quality management may include information such as:</p> <ul style="list-style-type: none"> • A description of the monitoring activities, including their nature, timing and extent; • Findings from the monitoring activities and deficiencies identified; and • The network’s evaluation of the root cause(s) of the identified deficiencies, the assessed effect of the deficiencies and recommended remedial actions.
<p><i>Monitoring Activities Undertaken by the Network Across the Network Firms</i></p> <p>61. The firm shall:</p> <p>(a) Understand the overall scope of the monitoring activities undertaken by the network across the network firms, including monitoring activities to determine that network requirements have been appropriately implemented across the network firms, and how the network will communicate the results of its monitoring activities to the firm;</p> <p>(b) At least annually, obtain information from the network about the overall results of the monitoring activities undertaken by the network across the network firms, if applicable, and communicate the information to engagement teams and other individuals, as appropriate, to enable them to take prompt and appropriate action in accordance with their responsibilities; and (Ref: Para. A201–A202A)</p>	<p><i>Monitoring Activities Undertaken by the Network Across the Network Firms</i> (Ref: Para. 61)</p> <p>A201. The information from the network about the overall results of the monitoring activities it undertakes across the network firms’ systems of quality management may be an aggregation or summary of the information described in paragraph A200, including trends and common areas of identified deficiencies across the network, or positive outcomes that may be replicated across the network. Such information may:</p> <ul style="list-style-type: none"> • Be used by the firm: <ul style="list-style-type: none"> • In identifying and assessing quality risks. • As part of other relevant information considered by the firm in determining whether deficiencies exist in the network requirements or network services used by the firm in its system of quality management. • Be communicated to group engagement partners, in the context of considering the competence and capabilities of component auditors from a firm within the network who are subject to common network requirements (e.g., common quality objectives, quality risks and responses). <p>A202. In some circumstances, the firm may obtain information from the network about deficiencies identified in a network firm’s system of quality management that affects the firm. The network may also gather information from the network firms regarding the results of external inspections over the network firms’ systems of quality management. In some instances, law or regulation in a particular jurisdiction may</p>

<p>(c) Based on the understanding, and if applicable, the information provided by the network, consider the effect of the monitoring activities undertaken by the network across the network firms on the firm’s system of quality management. (Ref: Para. A201)</p>	<p>prevent the network from sharing information with other firms within the network or may restrict the specificity of such information.</p> <div data-bbox="982 285 1955 483" style="border: 1px solid black; padding: 5px;"> <p><i>Example of when information about another network firm’s system of quality management affects the firm</i></p> <p>Another network firm performs work for the firm’s engagements, such as in the capacity of a component auditor.</p> </div> <p>A202A. In circumstances when the network does not provide the information about the overall results of the monitoring activities undertaken by the network across the network firms, the firm may take further actions, such as:</p> <ul style="list-style-type: none"> • Discussing the matter with the network; and • Determining the effect on the firm’s engagements, and communicating the effect to engagement teams.
<p><i>Deficiencies in Network Requirements or Network Services Identified by the Firm</i></p> <p>62. If the firm identifies a deficiency in the network requirements or network services, the firm shall: (Ref: Para. A203–A204)</p> <p>(a) Communicate to the network relevant information about the identified deficiency; and</p> <p>(b) In accordance with paragraph 49, design and implement remedial actions to address the effect of the identified deficiencies in the network requirements or network services.</p>	<p><i>Deficiencies in Network Requirements or Network Services Identified by the Firm</i> (Ref: Para. 62)</p> <p>A203. As network requirements or network services used by the firm form part of the firm’s system of quality management, they are also subject to the requirements of this ISQM regarding monitoring and remediation. The network requirements or network services may be monitored by the network, the firm, or a combination of both.</p> <div data-bbox="982 1045 1955 1284" style="border: 1px solid black; padding: 5px;"> <p><i>Example of when a network requirement or network service is monitored by both the network and the firm</i></p> <p>A network undertakes monitoring activities at a network level for a common methodology. The firm also monitors the methodology through the performance of engagement inspections.</p> </div> <p>A204. In designing and implementing the remedial actions to address the effect of the identified deficiencies in the network requirements or network services, the firm may:</p>

	<ul style="list-style-type: none"> • Understand the planned remedial actions by the network, including whether the firm has any responsibilities for implementing the remedial actions; and • Consider whether supplementary remedial actions need to be taken by the firm to address the identified deficiencies and their related root cause(s). <div data-bbox="982 391 1955 678" style="border: 1px solid black; padding: 5px;"> <p><i>Example of circumstances when supplementary remedial actions may be needed by the firm to address an identified deficiency in a network requirement or network service</i></p> <ul style="list-style-type: none"> • The network has not taken appropriate remedial actions. • The network's remedial actions will take time to effectively address the identified deficiency. </div>
<p>Evaluating the System of Quality Management</p>	<p>Evaluating the System of Quality Management (Ref: Para. 65A–65D)</p>
<p>65A. The individual(s) assigned ultimate responsibility and accountability for the system of quality management shall evaluate the system of quality management. The evaluation shall be undertaken as of a point in time, and shall be performed at least annually. (Ref: Para. A209A–A209C)</p> <p>65AA. Based on the evaluation, the individual(s) assigned ultimate responsibility and accountability for the system of quality management shall conclude whether the system of quality management provides the firm with reasonable assurance that the objectives of the system of quality management are being achieved. (Ref: Para. A210D–A210DA)</p>	<p>A209A. The firm remains responsible and accountable for achieving the objectives of this ISQM. Nevertheless, the evaluation of the system of quality management reinforces the responsibility and accountability of the individual(s) assigned ultimate responsibility and accountability for the system of quality management.</p> <p>A209B. The point in time at which the evaluation is undertaken may depend on the circumstances of the firm, and may coincide with the fiscal year end of the firm or the completion of an annual monitoring cycle. The evaluation may be undertaken more frequently than annually, such as in circumstances when the identified deficiencies are of a severity and pervasiveness that indicate that the system may not be providing reasonable assurance that the objectives of the system have been achieved.</p> <div data-bbox="909 1211 1955 1393" style="border: 1px solid black; padding: 5px;"> <p>A209C. <i>Scalability examples to demonstrate how the information to support the evaluation of the system of quality management may be obtained</i></p> <ul style="list-style-type: none"> • In a less complex firm, the individual(s) assigned ultimate responsibility and accountability for the system of quality management may be directly </div>

involved in the monitoring and remediation and will therefore be aware of the information that supports the evaluation of the system of quality management.

- In a more complex firm, the firm may need to establish processes to collate, summarize and communicate the information needed to evaluate of the system of quality management.

A210A. In the context of this ISQM, it is intended that the operation of the system as a whole provides the firm with reasonable assurance that the objectives of the system of quality management are being achieved. In concluding whether the system of quality management provides the firm with reasonable assurance that the objectives of the system of quality management are being achieved, the individual(s) assigned ultimate responsibility and accountability for the system of quality management may use the results of the firm's monitoring and remediation process and consider the following:

- The severity and pervasiveness of identified deficiencies, and the effect on the achievement of the objectives of the system of quality management;
- Whether identified deficiencies have been remediated, or are being actively remediated (i.e., whether the actions taken thus far by the firm to remediate the identified deficiencies are appropriate, including whether remedial actions have been designed and implemented); and
- Whether the effect of identified deficiencies on the system of quality management have been appropriately corrected, such as whether further actions have been taken in accordance with paragraph 51.

Example of the evaluation and conclusion at a point in time of whether the system of quality management provides the firm with reasonable assurance that the objectives of the system of quality management are being achieved

- When identified deficiencies are severe and pervasive, have not been remediated or actively remediated, and the effect of the deficiencies have

	<p>not been appropriately corrected, it may be determined that the system does not provide reasonable assurance that the objectives of the system of quality management are being achieved. A deficiency may be considered severe and pervasive when, for example, it relates to the firm’s governance and leadership, and affects the overall environment that supports the operation of the system of quality management.</p> <ul style="list-style-type: none"> • When identified deficiencies are severe but not pervasive, have not been remediated or actively remediated, and the effect of the deficiencies have not been appropriately corrected, it may be determined that, except for the matters to which the deficiencies relate, the system nevertheless provides the firm with reasonable assurance that the objectives of the system of quality management are being achieved. A deficiency may be considered severe but not pervasive when, for example, there is a technological failure in the firm’s IT application for accepting and continuing client relationships and specific engagements that results in the firm performing an engagement that would otherwise not have been accepted. <p>A210DA. This ISQM does not require the firm to obtain an independent assurance report on its system of quality management.</p>
<p>65C. If the evaluation indicates that the system of quality management does not provide the firm with reasonable assurance that the objectives of the system are being achieved, the individual(s) assigned ultimate responsibility and accountability for the system of quality management shall:</p> <p>(a) Take prompt and appropriate action in accordance with their responsibilities; and (Ref: Para. A210DB)</p> <p>(b) Communicate to:</p>	<p>A210DB. Prompt and appropriate action when the evaluation indicates that the system of quality management does not provide the firm with reasonable assurance that the objectives of the system are being achieved may include:</p> <ul style="list-style-type: none"> • Taking measures to support the performance of engagements and confirm that reports issued by the firm are appropriate in the circumstances, until such time as the identified deficiencies are remediated, and communicating such measures to engagement teams. • Obtaining legal advice.

<p>(i) Engagement teams and other individuals to the extent that it is relevant to their responsibilities; and (Ref: Para. A210DC)</p> <p>(ii) External parties in accordance with the firm’s policies or procedures required by paragraph 40(c)(iv). (Ref: Para. A210DD)</p>	<p>A210DC. In some circumstances the firm may have an independent governing body that has non-executive oversight of the firm. In such circumstances, communications may include informing the independent governing body.</p> <p>A210DD. <i>Examples of circumstances when it may be appropriate for the firm to communicate to external parties</i></p> <ul style="list-style-type: none"> • When the firm belongs to a network. • When other firms in the network use the work performed by the firm, for example, in the case of a group audit. • When a report issued by the firm is determined by the firm to be inappropriate as a result of the failure of the system of quality management, and management or those charged with governance of the entity need to be informed. • When law or regulation requires the firm to communicate to an oversight authority or a regulatory body that the system does not provide the firm with reasonable assurance that the objectives of the system are being achieved.
<p>65D. The firm shall undertake periodic performance evaluations of the individual(s) assigned ultimate responsibility and accountability for the system of quality management, and the individual(s) assigned operational responsibility for the system of quality management. In doing so, the firm shall take into consideration the evaluation of the system of quality management. (Ref: Para. A210E–A210G)</p>	<p><i>Performance Evaluations</i> (Ref: Para. 65D)</p> <p>A210E. Periodic performance evaluations promote accountability. In considering the performance of these individuals, the firm may take into account:</p> <ul style="list-style-type: none"> • The results of the firm’s monitoring activities for aspects of the system of quality management that relate to the responsibility of the individual. In some circumstances, the firm may set targets for the individual and measure the results of the firm’s monitoring activities against those targets. • The actions taken by the individual(s) in response to identified deficiencies that relate to the responsibility of that individual, including the timeliness and effectiveness of such actions.

	<p><i>Scalability examples to demonstrate how the firm may undertake the performance evaluations</i></p> <ul style="list-style-type: none"> • In a less complex firm, the firm may engage a service provider to perform the evaluation, or the results of the firm’s monitoring activities may provide an indication of the performance of the individual(s). • In a more complex firm, the performance evaluations may be undertaken by an independent non-executive member of the firm’s governing body, or a special committee overseen by the firm’s governing body. <p>A210F.A positive performance evaluation may be rewarded through compensation, promotion and other incentives that focus on the individual’s commitment to quality, and reinforce accountability. On the other hand, the firm may take corrective actions to address a negative performance evaluation that may affect the firm’s achievement of its quality objectives.</p> <p>Public Sector Considerations</p> <p>A210G. In the case of the public sector, it may not be practicable to perform a performance evaluation of the individual assigned ultimate responsibility and accountability for the system of quality management, or to take actions to address the results of the performance evaluation, given the nature of the individual’s appointment. Nevertheless, performance evaluations may still be undertaken for other individuals in the firm who are assigned operational responsibility for aspects of the system of quality management.</p>
<p>Documentation</p> <p>66. The firm shall prepare documentation of its system of quality management that is sufficient to: (Ref: Para. A211–A213)</p> <p>(a) Support a consistent understanding of the system of quality management by personnel,</p>	<p>Documentation (Ref: Para. 66–69)</p> <p>A211. Documentation provides evidence that the firm complies with this ISQM, as well as law, regulation or relevant ethical requirements. It may also be useful for training personnel, ensuring the retention of organizational knowledge and providing a history of the basis for decisions made by the firm about its system of quality management. It is neither necessary nor practicable for the firm to document every</p>

<p>including an understanding of their roles and responsibilities with respect to the firm's system of quality management;</p> <p>(b) Support the consistent implementation and operation of the responses; and</p> <p>(c) Provide evidence of the design, implementation and operation of the responses, to support the evaluation of the system of quality management by the individual(s) assigned ultimate responsibility and accountability for the system of quality management.</p>	<p>matter considered, or judgment made, about its system of quality management. Furthermore, compliance with this ISQM may be evidenced by the firm through its information and communication component, documents or other written materials, or IT applications that are integral to the components of the system of quality management.</p> <p>A212. Documentation may take the form of formal written manuals, checklists and forms, may be informally documented (e.g., e-mail communication or postings on websites), or may be held in IT applications or other digital forms (e.g., in databases). Factors that may affect the firm's judgments about the form, content and extent of documentation, including how often documentation is updated, may include:</p> <ul style="list-style-type: none"> • The complexity of the firm and the number of offices; • The nature and complexity of the firm's practice and organization; • The nature of engagements the firm performs and the nature of the entities for whom engagements are performed; • The extent to which the documentation may be reviewed by an external party, such as a professional, legal or regulatory body; • Whether the documentation would support an understanding of the system of quality management by an individual who is knowledgeable of matters related to quality management; • The nature and complexity of the matter being documented, such as whether it relates to an aspect of the system of quality management that has changed or an area of greater quality risk, and the complexity of the judgments relating to the matter; and • The frequency and extent of changes in the system of quality management. <p>In a smaller firm, it may not be necessary to have documentation supporting matters communicated because informal communication methods may be effective.</p>
--	---

	<p>Nevertheless, the firm may determine it appropriate to document such communications in order to provide evidence that they occurred.</p> <p>A213. In some instances, an external oversight authority may establish documentation requirements, either formally or informally, for example, as a result of the outcome of external inspection findings. Relevant ethical requirements may also include specific requirements addressing documentation, for example, the IESBA Code requires documentation of particular matters, including certain situations related to conflicts of interest, non-compliance with laws and regulations and independence.</p>
<p>67. The firm shall prepare documentation that includes:</p> <ul style="list-style-type: none"> (a) The identification of the individual(s) assigned ultimate responsibility and accountability for the system of quality management and operational responsibility for the system of quality management; (b) The firm's quality objectives and assessed quality risks; (Ref: Para. A214) (c) A description of the responses and how the firm's responses address the assessed quality risks; (d) Regarding the monitoring and remediation process: <ul style="list-style-type: none"> (i) Evidence of the monitoring activities performed; (ii) The evaluation of findings, and identified deficiencies and their related root cause(s); (iii) Remedial actions to address identified deficiencies and the evaluation of the 	<p>A214. In documenting the assessed quality risks, the firm may document the reasons for the assessment of the quality risks.</p>

<p>design and implementation of such remedial actions;</p> <p>(iv) Communications about monitoring and remediation; and</p> <p>(e) The basis for the conclusion whether the system of quality management provides the firm with reasonable assurance that the objectives of the system of quality management are being achieved.</p>	
<p>68. The firm shall document the matters in paragraph 67 as they relate to network requirements or network services and the evaluation of the network requirements or network services in accordance with paragraph 59(b). (Ref: Para. A215)</p>	<p>A215. The documentation may be provided by the network.</p>
<p>69. The firm shall establish a period of time for the retention of documentation for the system of quality management that is sufficient to enable the firm to monitor the design, implementation and operation of the firm's system of quality management, or for a longer period if required by law or regulation.</p>	



AUASB Board Meeting Summary Paper

AGENDA ITEM NO. **4.0**

Meeting Date: 10 March 2020

Subject: ISQM 2

Date Prepared: 4 March 2020

Action Required

For Information Purposes Only

A. Background

1. At the December 2019 IAASB meeting, the Board generally supported the Task Force’s proposed revisions relating to the scope of engagements subject to an EQR. Although some Board members expressed support for retaining the separate category of ‘due to the nature and circumstances of the engagement or the entity,’ other Board members questioned how that category differs from the category of engagements for which an EQR may be appropriate in response to assessed quality risks.

2. **What the Audit Technical Group (ATG) is seeking from the AUASB at the March 2020 AUASB meeting**
 - (a) Obtain the Board’s views about the recommendation of the ISQM 2 Task Force (TF) relating to engagements subject to an engagement quality review (EQR) in accordance with paragraph 41A(e) (previously paragraph 41A(c)) of proposed ISQM 1; and
 - (b) Obtain the Board’s feedback on the revised draft of proposed ISQM 2 at Agenda Item 4.1

The TF intends to update the draft of proposed ISQM 2 during the March 2020 IAASB meeting for Board members’ comments. It is proposed that the draft of proposed ISQM 2 as presented in March 2020, amended as appropriate for any final comments, be treated as the final text except for:

- Changes to align with revisions made to the drafts of proposed ISQM 1 and ISA 220 (Revised) and the Exposure Draft (ED) of proposed ISA 600 (Revised); and
- Any final coordination matters with IESBA Representatives.

This document contains preliminary views and/or AUASB Technical Group recommendations to be considered at a meeting of the AUASB, and does not necessarily reflect the final decisions of the AUASB. No responsibility is taken for the results of actions or omissions to act on the basis of reliance on any information contained in this document (including any attachments), or for any errors or omissions in it.

After the March 2020 meeting, the TF will focus on:

- Addressing comments received from the Board in March 2020, as well as feedback received from outreach activities with stakeholders and coordination activities with the ISQM 1, ISA 220 and ISA 600 Task Forces and IESBA Representatives.
- The conforming and consequential amendments to the ISAs arising from proposed ISQM 2.

The Task Force will work towards the final approval of proposed ISQM 2 as planned at the June 2020 IAASB meeting.

In section D.1 – D.2 the ATG has highlighted the taskforces current thinking on the above areas. The ATG have highlighted (in a box) the questions that the IAASB will consider at the forthcoming March 2020 IAASB meeting. In line with the AUASB international influencing strategy, AUASB members are encouraged to comment on any of these questions to inform the AUASB Chair of their views.

3. **Matters Raised at the December IAASB Meeting**

Scope of Engagements subject to an EQR

The TF noted comments from several Board members that the separate category of engagements subject to an EQR due to the ‘nature and circumstances of the engagement or the entity’ was confusing due to the introduction at the December 2019 IAASB meeting of ‘quality risk considerations’ in proposed ISQM 1. Those quality risk considerations (now referred to as ‘factors’ in the draft of proposed ISQM 1) included *the nature and circumstances of the firm*, and *the nature and circumstances of the engagements* (emphasis added).

As part of a firm’s risk assessment process (FRAP) in identifying and assessing quality risks to provide a basis for the design and implementation of responses (see paragraph 22E(a) of proposed ISQM 1), the firm is required to understand factors that may adversely affect the achievement of its quality objective.

In addition to the similarity of the wording of the separate category to the wording of the factors in the FRAP in proposed ISQM 1, some also may hold the view that a separate category that is not in response to assessed quality risks is inconsistent with the underlying principle of a firm’s system of quality management that requires the firm to apply a ‘*risk-based approach*’ (emphasis added), as provided in paragraphs 9A-10 of proposed ISQM 1. Consequently, requiring an EQR in response to reasons that are not risk-based is inconsistent with, and may be viewed as undermining the principle of a risk-based

approach in proposed ISQM 1. Extracts of paragraphs 9A-10 of proposed ISQM 1 are shown below for reference.

9A. This ISQM requires the firm to apply a risk-based approach in designing, implementing and operating the components of the system of quality management in an interconnected and coordinated manner such that the quality of engagements is proactively managed by the firm. (Ref: Para. A4A)

10. The risk-based approach is embedded in the requirements of this ISQM through:

- (a) Establishing quality objectives. The quality objectives established by the firm consist of objectives in relation to the components of the system of quality management that are to be achieved by the firm. The firm is required to establish the quality objectives set out in this ISQM and any additional quality objectives beyond those specified by this ISQM that are considered necessary by the firm to achieve the objectives of the system of quality management.
- (b) Identifying and assessing risks to the achievement of the quality objectives (referred to in this standard as quality risks). The firm is required to identify and assess quality risks to provide a basis for designing and implementing responses.
- (c) Designing and implementing responses to address the assessed quality risks. The nature, timing and extent of the firm's responses to address the assessed quality risks are based on, and responsive to, the reasons for the assessments given to the quality risks.

In view of the comments from Board members during the December 2019 meeting, the TF recommends that the **separate category of 'due to the nature and circumstances of the engagement or the entity' be absorbed into the broader category of engagements** for which the firm determines an EQR is an appropriate response to assessed quality risks.

The TF does not consider that absorbing this separate category would significantly affect the number of engagements subject to EQR since relevant aspects of the application material (i.e., factors to be considered in identifying engagements subject to an EQR due to the nature and circumstances of the engagement or the entity) have been incorporated into the application material for the broader category of engagements subject to an EQR as an appropriate response to assessed quality risks (now part of paragraph A153I in ISQM1).

Refer D.1 for further discussion.

Objectivity and Cooling-Off Period

With respect to objectivity, including a cooling-off period for individuals moving into the role of EQR after having served as the engagement partner:

- The Board generally supported the TF's proposal to address matters of objectivity and cooling-off in ISQM 2.
- Some Board members also supported a mandatory cooling-off period in ISQM 2.

- While Board members noted a preference for objectivity and cooling-off period to be addressed in the IESBA Code and applauded the IESBA’s willingness to address it, Board members, however, expressed views about the respective timelines of the two Boards (i.e., whether IESBA’s due process would result in changes to the IESBA Code being finalised by the time the IAASB’s quality management standards are expected to be finalised in June 2020).
- Hence, Board members supported the IAASB moving forward based on the task force’s initial recommendations, with a clear understanding of the need for close coordination and cooperation to make sure that the two Boards are not moving down separate paths on this issue (the hope is to keep the paths aligned as closely as possible to ensure that the IAASB standards and the IESBA Code are complementary and not inconsistent).
- Board members also raised concerns regarding jurisdictions where the IESBA Code is not adopted, but the ISAs are, and why this may necessitate ISQM 2 to address cooling-off.
- There was also support for the TF to further consider extending the cooling-off requirement to all engagements for which an EQR review is required (i.e., not just for listed entities or PIEs), and to consider whether a cooling-off period should also extend to other individuals in the engagement (e.g., key audit partners).
- Discussions were also held since December 2019 to update IESBA Representatives and Staff about the recommendations of the TF relating to engagements subject to an EQR, and relating to the objectivity, including a mandatory cooling-off period, for an individual being appointed as an EQR after previously serving as the engagement partner. The rationale for the proposed revisions resulting from these discussions (as reflected in Agenda Item 4.1) are explained further below.

Refer to D.2 for further discussion.

EQR for Group Audit

Respondents had comments or questions about how the requirements and guidance in proposed ISQM 2 would be applied in the context of group audits.

For a group audit engagement, the TF view is that the focus of the EQR are those significant judgments relating to the group financial statements, which may relate to significant judgments made at one or more components. In this regard, the performance of an EQR for a group audit engagement may involve additional considerations by the EQR depending on the size and complexity of the group. For larger, more complex group audits, the EQR may need to discuss significant matters and significant judgments with other key members of the engagement team (e.g., the partners or other individuals responsible for performing audit procedures on the financial information of a component). In these circumstances, it may be appropriate for the EQR to be assisted by an individual or team of individuals, either internal or external, with the relevant expertise, in accordance with paragraph 17 of the standard, including, when applicable, individuals appointed to perform an EQR of a component.

New application material (see paragraph A28A) was added to provide guidance for group audit considerations in an EQR as described above. This proposed guidance reflects discussions with the ISA 600 TF, and any further changes will be coordinated with that TF.

Proposed revisions relating to the application material in proposed ISQM 2 regarding considerations for an EQR for a group audit (as reflected in Agenda Item 4.1) were discussed with the ISA 600 Task Force. The ISA 600 TF was supportive of these proposed revisions.

The ATG are also supportive of the proposed revisions in relation to Group Audit.

4. **The way forward:**

The IAASB has indicated that the timing for approval of these QM standards to be June 2020.

In general, there was support for establishing a system of quality management, including the new quality management approach (QMA), and strong support for EQRs as a response, among others, that is designed and implemented by the firm to address quality risks.

D.1 Scope of Engagements subject to an EQR

1. Accordingly, the TF has made the following proposed revisions:

- Absorbed the separate category of ‘due to the nature and circumstances of the engagement or the entity’ into the broader category of engagements for which the firm determines that an EQR is an appropriate response to assessed quality risks in paragraph 41A(e) of proposed ISQM 1.
- Redrafted the lead-in wording in paragraph A153I (previously paragraph A104) to provide a link to the FRAP with respect to the:
 - Factors (see paragraph 22E(a)(ii) of proposed ISQM 1) relating to the nature and circumstances of the engagements performed by the firm that may adversely affect the achievement of its quality objectives, which the firm is required to understand when identifying and assessing quality risks; and
 - Conditions and circumstances that may lead the firm to determine that an EQR is the appropriate response in designing and implementing responses to address assessed quality risks relating to the quality objectives of engagement performance.
- Aligned paragraph A153I with the ISQM 1 TF’s approach of presenting the examples of such conditions and circumstances in boxes. In addition, the conditions and circumstances in paragraph A153I of proposed ISQM 1 are now further subdivided into:
 - Conditions and circumstances relating to the types and characteristics of engagements performed; and
 - Conditions and circumstances relating to the types of entities for which engagements are undertaken.

ATG Views

The ATG agree with the proposed changes to 41A(e) to better align with the FRAP and in identifying and assessing quality risks to provide a basis for the design and implementation of responses in proposed ISQM 1, the firm is required to understand factors that may adversely affect the achievement of its quality objectives.

The examples in A153I are also useful in determining conditions and circumstances relating to types of entities and engagements performed or undertaken.

Matter for IAASB Consideration

1. Does the IAASB support the proposed changes to the requirements in paragraph 41A(e) of proposed ISQM 1 and related application material relating to the scope of engagements subject to an EQR?

D2. Objectivity and Cooling-Off Period

The Board generally supported the TF's proposal to address objectivity and include a cooling-off period in proposed ISQM 2 for individuals moving into the role of EQR after serving as the engagement partner. However, some Board members did not support a mandatory cooling-off period in ISQM 2, or supported flexibility for firms to develop policies and procedures to determine an appropriate cooling-off period.

While indicating a preference for objectivity and cooling-off period to be addressed in the IESBA Code and applauding the IESBA's willingness to address these matters, Board members expressed views about whether the time needed for IESBA's due process would result in changes to the IESBA Code by the expected finalization of the IAASB's quality management standards in June 2020.

Since December 2019, IESBA have agreed to provide guidance addressing objectivity of the EQR in the Code. IESBA have proposed the guidance be included in section 120 of the Code. Section 120 sets out the conceptual framework. The fundamental principles, of which objectivity is one, are addressed in section 110 with objectivity being discussed in subsection 112.

Mandatory Cooling-Off Period

The TF continues to believe strongly that a mandatory cooling-off period is in the public interest, and is the most appropriate approach to drive consistency in practice, while awaiting the outcome of the IESBA's planned activities to address this matter in the IESBA Code. The objectivity of the EQR is an important aspect of the requirements regarding the eligibility of that individual to be appointed to that role by the firm. As has been noted in previous discussions with the IAASB on this topic, it is the separation from the previous involvement in making significant judgments as the engagement partner that is necessary for the EQR to objectively evaluate the significant judgments made by the engagement team, and the conclusions reached thereon.

Accordingly, the TF has included a requirement in paragraph 16A:

16A. The firm's policies or procedures established in accordance with paragraph 16(b) shall address threats to objectivity created by an individual being appointed as an EQR after previously serving as the engagement partner. Such policies or procedures shall specify a cooling-off period of two years, or a longer period if required by relevant ethical requirements, before an engagement partner can assume the role of EQR. (Ref: Para. A17A–A17C)

The TF also has the view that a mandatory cooling-off period is consistent with the fundamental principles of, and the conceptual framework in, the IESBA Code.

The TF believes that the requirement should apply to all engagements for which an EQR is performed. The view of the TF is that threats to the objectivity of an engagement partner stepping into the role of EQR are not unique to audits of listed entities only, or to the type of engagement. In reaching this conclusion, the TF noted that other than for audits of listed entities or when required by law or regulation, EQRs are not mandated for other engagements, and the firm may employ responses other than an EQR to address assessed quality risks.

ATG Views

The ATG agree that:

- a. A mandatory cooling-off period as specified in para 16A is in the public interest and is likely to drive consistency in practice however the AUASB’s view as stated in our submission to IAASB was for this issue to be dealt with in the IESBA Code.
- b. The ATG supports IESBA’s objective to provide guidance addressing the objectivity of the EQR. However, the AUASB as stated in their submission on ISQM 2 has concerns about the cooling off requirement for an engagement partner moving to an EQR role being addressed in IAASB’s QM standards including if any a specified cooling off period. Rather the AUASB strongly encourages IESBA to fully consider the issue and if necessary, include a requirement in the Code alongside the auditor rotation requirements in Section 540 of the Code.

Matter for IAASB Consideration

1. The IAASB is asked for its views on the changes to proposed ISQM 2 as presented in Agenda Item 5-E.

Material Presented

- | | |
|-----------------|---|
| Agenda Item 4.0 | AUASB Board Meeting Summary Paper |
| Agenda Item 4.1 | Proposed ISQM 2 – IAASB Agenda 5E (Clean) |

Action Required

No.	Action Item	Responsibility	Due Date
1.	Provide feedback to ATG on key issues noted on ISQM 2 and proposed draft ISQM 2.	AUASB	11 Mar 2020

Proposed ISQM 2, Engagement Quality Reviews – Draft (Clean)

This paper is a complete clean draft of proposed ISQM 2, which incorporates the proposed changes made by the Task Force in response to the comments received during the December 2019 IAASB meeting and the written comments received thereafter.

CONTENTS

[Content Page to be Inserted]

Proposed International Standard on Quality Management (ISQM) 2, *Engagement Quality Reviews*, should be read in conjunction with Proposed ISQM 1, *Quality Management for Firms that Perform Audits or Reviews of Financial Statements, or Other Assurance or Related Services Engagements*.

ISQM 2 Requirement	Application and Other Explanatory Material
Introduction	
Scope of this ISQM	
1. This International Standard on Quality Management (ISQM) deals with: <ul style="list-style-type: none"> • The appointment and eligibility of the engagement quality reviewer; and • The engagement quality reviewer’s responsibilities relating to the performance and documentation of an engagement quality review. 	
2. This ISQM applies to all engagements for which an engagement quality review is required to be performed in accordance with proposed ISQM 1. ¹ This ISQM is premised on the basis that the firm is subject	

¹ Proposed International Standard on Quality Management (ISQM) 1 (Previously International Standard on Quality Control 1), *Quality Management for Firms that Perform Audits or Reviews of Financial Statements, or Other Assurance or Related Services Engagements*, paragraph 41A(e)

ISQM 2 Requirement	Application and Other Explanatory Material
<p>to proposed ISQM 1 or to national requirements that are at least as demanding.</p>	
<p>2A. An engagement quality review performed in accordance with this ISQM is a specified response that is designed and implemented by the firm in accordance with proposed ISQM 1.² The performance of an engagement quality review is undertaken at the engagement level by the engagement quality reviewer on behalf of the firm.</p>	
<p><i>Scalability</i></p>	
<p>2B. The nature, timing and extent of the engagement quality reviewer’s procedures required by this ISQM vary depending on the nature and circumstances of the engagement. For example, the engagement quality reviewer’s procedures would normally be less extensive for engagements involving fewer significant judgments made by the engagement team.</p>	
<p>The Firm’s System of Quality Management and Role of Engagement Quality Reviews</p>	
<p>3. Proposed ISQM 1 establishes the firm’s responsibilities for its system of quality management and requires the firm to design and implement responses to assessed quality risks related to engagement performance. Such responses include establishing policies or procedures addressing engagement quality reviews in accordance with this ISQM.</p>	

² Proposed ISQM 1, paragraph 41A(e)

ISQM 2 Requirement	Application and Other Explanatory Material
<p>4. The objective of the firm is to design, implement and operate a system of quality management for audits or reviews of financial statements, or other assurance or related services engagements performed by the firm, that provides the firm with reasonable assurance that:</p> <p>(a) The firm and its personnel fulfill their responsibilities in accordance with professional standards and applicable legal and regulatory requirements, and conduct engagements in accordance with such standards and requirements; and</p> <p>(b) Engagement reports issued by the firm or engagement partners are appropriate in the circumstances.³</p>	
<p>5. The public interest is served by the consistent performance of quality engagements. Quality engagements are achieved through planning and performing engagements and reporting on them in accordance with professional standards and applicable legal and regulatory requirements. Achieving the objectives of those standards and complying with the requirements of applicable law or regulation involves exercising professional judgment and, when applicable to the nature and circumstances of the engagement, exercising professional skepticism.</p>	
<p>6. An engagement quality review is an objective evaluation</p>	

³ Proposed ISQM 1, paragraph 18

ISQM 2 Requirement	Application and Other Explanatory Material
<p>of the significant judgments made by the engagement team, and the conclusions reached thereon. The engagement quality reviewer’s evaluation of significant judgments is performed in the context of professional standards and applicable legal and regulatory requirements. However, an engagement quality review is not intended to be an evaluation of whether the entire engagement complies with professional standards and applicable legal and regulatory requirements, or with the firm’s policies or procedures.</p>	
<p>7. The engagement quality reviewer is not a member of the engagement team. The performance of an engagement quality review does not change the responsibilities of the engagement partner for the direction and supervision of the members of the engagement team and the review of their work. The engagement quality reviewer is not required to obtain evidence to support the opinion or conclusion on the engagement, but the engagement team may obtain further evidence in responding to matters raised during the engagement quality review.</p>	
<p>Authority of this ISQM</p>	
<p>8. This ISQM contains the objective for the firm in following this ISQM, and requirements designed to enable the firm and the engagement quality reviewer to meet that stated objective. In addition, it contains related guidance in the form of application and other explanatory material and introductory material that provides context relevant to a proper understanding of this ISQM, and definitions.</p>	

ISQM 2 Requirement	Application and Other Explanatory Material
<p>Proposed ISQM 1⁴ explains the terms objective, requirements, application material and other explanatory material, introductory material, and definitions.</p>	
Effective Date	
<p>9. This ISQM is effective for:</p> <p>(a) Audits and reviews of financial statements for periods beginning on or after [Date]; and</p> <p>(b) Other engagements beginning on or after [Date].</p>	
Objective	
<p>10. The objective of the firm, through appointing an eligible engagement quality reviewer, is to perform an objective evaluation of the significant judgments made by the engagement team and the conclusions reached thereon.</p>	
Definitions	
<p>11. In this ISQM, the following terms have the meanings attributed below:</p> <p>(a) Engagement quality review – An objective evaluation of the significant judgments made by the engagement team and the conclusions reached thereon, performed by the engagement quality reviewer and completed on or before the date of the engagement report.</p>	

⁴ Proposed ISQM 1, paragraphs A6–A9

ISQM 2 Requirement	Application and Other Explanatory Material
<p>(b) Engagement quality reviewer – A partner, other individual in the firm, or an external individual appointed by the firm to perform the engagement quality review.</p> <p>(c) Relevant ethical requirements – Principles of professional ethics and ethical requirements that are applicable to a professional accountant when undertaking an engagement quality review. Relevant ethical requirements ordinarily comprise the provisions of the International Ethics Standards Board for Accountants’ <i>International Code of Ethics for Professional Accountants (including International Independence Standards)</i> (IESBA Code) related to audits or reviews of financial statements, or other assurance or related services engagements, together with national requirements that are more restrictive.</p>	
Requirements	
Applying, and Complying with, Relevant Requirements	
<p>12. The firm and the engagement quality reviewer shall have an understanding of this ISQM, including the application and other explanatory material, to understand the objective of this ISQM and to properly apply the requirements relevant to them.</p>	
<p>13. The firm or the engagement quality reviewer, as applicable, shall comply with each requirement of this ISQM, unless the requirement is not relevant in the</p>	

ISQM 2 Requirement	Application and Other Explanatory Material
<p>circumstances of the engagement.</p>	
<p>14. The proper application of the requirements is expected to provide a sufficient basis for the achievement of the objective of this standard. However, if the firm or the engagement quality reviewer determines that the application of the relevant requirements does not provide a sufficient basis for the achievement of the objective of this standard, the firm or the engagement quality reviewer, as applicable, shall take further actions to achieve the objective.</p>	
<p>Appointment and Eligibility of Engagement Quality Reviewers</p>	
	<p><i>Assignment of Responsibility for the Appointment of Engagement Quality Reviewers (Ref: Para. 15)</i></p>
<p>15. The firm shall establish policies or procedures that require the assignment of responsibility for the appointment of engagement quality reviewers to an individual(s) with the competence, capabilities and appropriate authority within the firm to fulfill the responsibility. Those policies or procedures shall require such individual(s) to appoint the engagement quality reviewer. (Ref: Para. A1–A3)</p>	<p>A1. Competence and capabilities that are relevant to an individual's ability to fulfill responsibility for the appointment of the engagement quality reviewer may include appropriate knowledge about:</p> <ul style="list-style-type: none"> • The responsibilities of an engagement quality reviewer; • The criteria in paragraphs 16 and 16A regarding the eligibility of engagement quality reviewers; and • The nature and circumstances of the engagement or the entity subject to an engagement quality review, including the composition of the engagement team. <p>A2. The firm may assign more than one individual to be responsible for appointing engagement quality reviewers. For example, the firm's policies or procedures may specify a different process for appointing engagement quality reviewers for audits of listed entities than for audits of non-listed entities or other engagements, with different individuals responsible for each process.</p>

ISQM 2 Requirement	Application and Other Explanatory Material
	<p>A3. In certain circumstances, it may not be practicable for an individual other than a member of the engagement team to appoint the engagement quality reviewer, for example, in the case of a smaller firm or a sole practitioner.</p>
	<p><i>Eligibility of the Engagement Quality Reviewer</i> (Ref: Para. 16)</p>
<p>16. The firm shall establish policies or procedures that set forth the criteria for eligibility to be appointed as an engagement quality reviewer. Those policies or procedures shall require that the engagement quality reviewer not be a member of the engagement team, and: (Ref: Para. A4)</p>	<p>A4. In some circumstances, for example, in the case of a smaller firm or a sole practitioner, there may not be a partner or other individual within the firm who is eligible to perform the engagement quality review. In these circumstances, the firm may contract with, or obtain the services of, external individuals to perform the engagement quality review. An external individual may be a partner or an employee of another firm within the firm's network or a service provider. When using such an external individual, the firm is subject to the requirements for network requirements or network services in paragraphs 58–62 of proposed ISQM 1, or the requirements for resources from service providers in paragraph 38 of proposed ISQM 1, respectively.</p>
<p>(a) Has the competence and capabilities, including sufficient time, and the appropriate authority to perform the engagement quality review; (Ref: Para. A6–A12)</p>	<p><i>Eligibility Criteria for the Engagement Quality Reviewer</i></p> <p>Competence and Capabilities, Including Sufficient Time (Ref: Para. 16(a))</p> <p>A6. Competence⁵ refers to the integration and application of technical competence, professional skills, and professional ethics, values and attitudes, and the appropriate experience relevant to the nature and circumstances of the engagement, including:</p> <ul style="list-style-type: none"> • An understanding of professional standards and applicable legal and regulatory requirements and of the firm's policies or procedures relevant to the engagement; • Knowledge of the entity's industry; • An understanding of, and experience relevant to, engagements of a similar nature and complexity; and

⁵ Proposed ISQM 1, paragraph A117

ISQM 2 Requirement	Application and Other Explanatory Material
	<ul style="list-style-type: none"> • An understanding of the responsibilities of the engagement quality reviewer in performing and documenting the engagement quality review, which may be attained or enhanced by receiving relevant training from the firm. <p>A7. An engagement quality review is a specified response to assessed quality risks relating to engagement performance. Accordingly, the factors considered by the firm in determining that an engagement quality review is an appropriate response to assessed quality risks⁶ may be an important consideration in the firm's determination of the competence and capabilities required to perform the engagement quality review for that engagement. Other considerations that the firm may take into account in determining whether the engagement quality reviewer has the competence and capabilities, including sufficient time, needed to evaluate the significant judgments made by the engagement team and the conclusions reached thereon include, for example:</p> <ul style="list-style-type: none"> • The nature of the entity. • The specialization and complexity of the industry or regulatory environment in which the entity operates. • The extent to which the engagement relates to matters requiring specialized expertise (e.g., with respect to information technology or specialized areas of accounting or auditing), or scientific and engineering expertise, such as may be needed for certain assurance engagements. Also see paragraph A18. <p>A8. In evaluating the competence and capabilities of an individual who may be appointed as an engagement quality reviewer, the findings arising from the firm's monitoring activities (e.g., findings from the inspection of in-process or completed engagements for which the individual was an engagement team member or engagement quality reviewer) or the results of external inspections may also be relevant considerations.</p> <p>A9. A lack of appropriate competence or capabilities affects the ability of the engagement quality reviewer to exercise appropriate professional judgment in performing the review.</p>

⁶ Proposed ISQM 1, paragraphs 41A(e)(iii) and A153I

ISQM 2 Requirement	Application and Other Explanatory Material
	<p>For example, an engagement quality reviewer who lacks relevant industry experience may not possess the ability or confidence necessary to evaluate and, where appropriate, challenge significant judgments made, and the exercise of professional skepticism, by the engagement team on a complex, industry-specific accounting or auditing matter.</p> <p>Appropriate Authority (Ref: Para. 16(a))</p> <p>A10. Actions at the firm level help to establish the authority of the engagement quality reviewer. For example, by creating a culture of respect for the role of the engagement quality reviewer, the engagement quality reviewer is less likely to experience pressure from the engagement partner or other personnel to inappropriately influence the outcome of the engagement quality review. In some cases, the engagement quality reviewer’s authority may be enhanced by the firm’s policies or procedures to address differences of opinion, which may include actions the engagement quality reviewer may take when a disagreement occurs between the engagement quality reviewer and the engagement team.</p> <p>A11. The authority of the engagement quality reviewer may be diminished when:</p> <ul style="list-style-type: none"> • The culture within the firm promotes respect for authority only of individuals at a higher level of hierarchy within the firm. • The engagement quality reviewer has a reporting line to the engagement partner, for example, when the engagement partner holds a leadership position in the firm or is responsible for determining the compensation of the engagement quality reviewer. <p>Public Sector Considerations</p> <p>A12. In the public sector, an auditor (e.g., an Auditor General, or other suitably qualified individual appointed on behalf of the Auditor General) may act in a role equivalent to that of the engagement partner with overall responsibility for public sector audits. In such circumstances, the selection of the engagement quality reviewer may include consideration of the need for independence and the ability of the engagement quality</p>

ISQM 2 Requirement	Application and Other Explanatory Material
	<p>reviewer to provide an objective evaluation.</p>
<p>(b) Comply with relevant ethical requirements, including in relation to threats to objectivity and independence of the engagement quality reviewer; and (Ref: Para. A13–A16)</p>	<p>Relevant Ethical Requirements (Ref: Para. 16(b))</p> <p>A13. The relevant ethical requirements that are applicable when undertaking an engagement quality review may vary, depending on the nature and circumstances of engagements subject to an engagement quality review. Various provisions of relevant ethical requirements may apply only to individual professional accountants, such as an engagement quality reviewer, and not the firm.</p> <p>A14. Relevant ethical requirements may include specific independence requirements that would apply to individual professional accountants, such as an engagement quality reviewer. Relevant ethical requirements may also include provisions that address threats to independence created by the long association of personnel with an audit or assurance client. In this regard, the application of any such provisions dealing with long association is distinct from, but may need to be taken into consideration in applying, the required cooling-off period in accordance with paragraph 16A of this ISQM.</p> <p>Threats to the Objectivity of the Engagement Quality Reviewer</p> <p>A15. Threats to the engagement quality reviewer’s objectivity may be created by a broad range of facts and circumstances. For example:</p> <ul style="list-style-type: none"> • A self-review threat may be created when the engagement quality reviewer previously was involved with significant judgments made by the engagement team, in particular as the engagement partner or other engagement team member. • A familiarity or self-interest threat may arise when the engagement quality reviewer is a close or immediate family member of the engagement partner or another member of the engagement team, or through close personal relationships with members of the engagement team. • An intimidation threat may be created when actual or perceived pressure is exerted on the engagement quality reviewer (e.g., when the engagement

ISQM 2 Requirement	Application and Other Explanatory Material
	<p>partner is an aggressive or dominant individual, or the engagement quality reviewer has a reporting line to the engagement partner).</p> <p>A16. Relevant ethical requirements may include requirements and guidance to identify, evaluate and address threats to objectivity. For example, the IESBA Code provides specific guidance, including examples of types of threats to objectivity in relation to circumstances in which a professional accountant is appointed as an engagement quality reviewer, factors that are relevant in evaluating the level of such threats, and safeguards or actions that might address such threats.</p>
<p>(c) Comply with provisions of law and regulation, if any, that are relevant to the eligibility of the engagement quality reviewer. (Ref: Para. A17)</p>	<p>Law or Regulation Relevant to Eligibility of the Engagement Quality Reviewer (Ref: Para. 16(c))</p> <p>A17. Law or regulation may prescribe additional requirements regarding the eligibility of the engagement quality reviewer. For example, in some jurisdictions, the engagement quality reviewer may need to possess certain qualifications or be licensed to be able to perform the engagement quality review.</p>
	<p><i>Cooling-Off Period for an Individual After Previously Serving as the Engagement Partner</i> (Ref: Para. 16A)</p>
<p>16A. The firm's policies or procedures established in accordance with paragraph 16(b) shall also address threats to objectivity created by an individual being appointed as an engagement quality reviewer after previously serving as the engagement partner. Such policies or procedures shall specify a cooling-off period of two years, or a longer period if required by relevant ethical requirements, before an engagement partner can assume the role of engagement quality reviewer. (Ref: Para. A17A–A17B)</p>	<p>A17A. In recurring engagements, the matters on which significant judgments are made often do not vary and therefore significant judgments made in prior periods may continue to affect judgments of the engagement team in subsequent periods. The ability of an engagement quality reviewer to perform an objective evaluation of significant judgments is therefore affected when the individual was previously involved with those judgments as the engagement partner. In such circumstances, it is important that appropriate safeguards are put in place to reduce threats to objectivity, in particular the self-review threat, to an acceptable level. Accordingly, this ISQM requires the firm to establish policies or procedures that specify a cooling-off period during which the</p>

ISQM 2 Requirement	Application and Other Explanatory Material
	<p>engagement partner is precluded from being appointed as the engagement quality reviewer.</p> <p>A17B. The firm’s policies or procedures also may address whether a cooling-off period is appropriate for an individual other than the engagement partner before becoming eligible to be appointed as the engagement quality reviewer on that engagement. In this regard, the firm may consider the nature of that individual’s role and previous involvement with the significant judgments made on the engagement. For example, the firm may determine that an engagement partner responsible for the performance of audit procedures on the financial information of a component in a group audit engagement may not be eligible to be appointed as the group engagement quality reviewer because of that audit partner’s involvement in the significant judgments affecting the group audit engagement.</p>
<p>17. The firm shall establish policies or procedures that set forth the criteria for eligibility of individuals who assist the engagement quality reviewer. Those policies or procedures shall require that such individuals not be members of the engagement team, and:</p>	
<p>(a) Have the competence and capabilities, including sufficient time, to perform the duties assigned to them; and (Ref: Para. A18)</p>	<p><i>Circumstances When the Engagement Quality Reviewer is Assisted by Other Individuals</i> (Ref: Para. 17–18)</p> <p>A18. In certain circumstances, it may be appropriate for the engagement quality reviewer to be assisted by an individual or team of individuals, either internal or external, with the relevant expertise. For example, highly specialized knowledge, skills or expertise may be useful for understanding certain transactions undertaken by the entity to help the engagement quality reviewer evaluate the significant judgments made by the engagement team related to those transactions.</p>
<p>(b) Comply with relevant ethical requirements, including in relation to threats to their objectivity and, if applicable, the provisions of law and</p>	<p>A18A. The guidance in paragraph A15 may be helpful to the firm when establishing policies or procedures that address threats to objectivity of individuals who assist the engagement quality reviewer.</p>

ISQM 2 Requirement	Application and Other Explanatory Material
regulation. (Ref: Para. A18A–A19)	A19. When the engagement quality reviewer is assisted by an external individual, the assistant's responsibilities, including those related to compliance with relevant ethical requirements, may be set out in the contract or other agreement between the firm and the assistant.
<p>18. The firm shall establish policies or procedures that:</p> <p>(a) Require the engagement quality reviewer to take overall responsibility for the performance of the engagement quality review; and</p> <p>(b) Address the engagement quality reviewer's responsibility for determining the nature, timing and extent of the direction and supervision of the work of individuals assisting in the review, and the review of their work. (Ref: Para. A19A)</p>	<p>A19A. The firm's policies or procedures may include responsibilities of the engagement quality reviewer to:</p> <ul style="list-style-type: none"> • Consider whether assistants understand their instructions and whether the work is being carried out in accordance with the planned approach to the engagement quality review; and • Address matters raised by assistants, considering their significance and modifying the planned approach appropriately.
<i>Impairment of the Engagement Quality Reviewer's Eligibility to Perform the Engagement Quality Review</i>	<i>Impairment of the Engagement Quality Reviewer's Eligibility to Perform the Engagement Quality Review</i> (Ref: Para. 19–20)
<p>19. The firm shall establish policies or procedures that address circumstances in which the engagement quality reviewer's eligibility to perform the engagement quality review is impaired and the appropriate actions to be taken by the firm, including the process for identifying and appointing a replacement in such circumstances. (Ref: Para. A20)</p>	<p>A20. Factors that may be relevant to the firm in considering whether the eligibility of the engagement quality reviewer to perform the engagement quality review is impaired include:</p> <ul style="list-style-type: none"> • Whether changes in the circumstances of the engagement result in the engagement quality reviewer no longer having the appropriate competence and capabilities to perform the review; • Whether changes in the other responsibilities of the engagement quality reviewer indicate that the individual no longer has sufficient time to perform the review; or • Notification from the engagement quality reviewer in accordance with paragraph 20.

ISQM 2 Requirement	Application and Other Explanatory Material
<p>20. When the engagement quality reviewer becomes aware of circumstances that impair the engagement quality reviewer's eligibility, the engagement quality reviewer shall notify the appropriate individual(s) in the firm, and: (Ref: Para. A21)</p> <p>(a) If the engagement quality review has not commenced, decline the appointment to perform the engagement quality review; or</p> <p>(b) If the engagement quality review has commenced, discontinue the performance of the engagement quality review.</p>	<p>A21. In circumstances in which the engagement quality reviewer's eligibility to perform the engagement quality review becomes impaired, the firm's policies or procedures may set out a process by which alternative eligible individuals are identified or may specify the period of time after notification within which the firm is required to appoint a replacement. The firm's policies or procedures may also address the responsibility of the individual appointed to replace the engagement quality reviewer to perform procedures sufficient to fulfill the requirements of this ISQM with respect to the performance of the engagement quality review. Such policies or procedures may further address the need for consultation in such circumstances.</p>
Performance of the Engagement Quality Review	Performance of the Engagement Quality Review (Ref: Para. 21–24)
<p>21. The firm shall establish policies or procedures regarding the performance of the engagement quality review that address:</p>	
<p>(a) The engagement quality reviewer's responsibilities to perform procedures in accordance with paragraphs 22–23 at appropriate points in time during the engagement to provide an appropriate basis for an objective evaluation of the significant judgments made by the engagement team and the conclusions reached thereon;</p>	
<p>(b) The responsibilities of the engagement partner in relation to the engagement quality review, including that the engagement partner is precluded from dating the engagement report until</p>	<p><i>Engagement Partner Responsibilities in Relation to the Engagement Quality Review</i> (Ref: Para. 21(b))</p>

ISQM 2 Requirement	Application and Other Explanatory Material
<p>notification has been received from the engagement quality reviewer in accordance with paragraph 24 that the engagement quality review is complete; and (Ref: Para. A22–A23)</p>	<p>A22. Proposed ISA 220 (Revised)⁷ establishes the requirements for the engagement partner in audit engagements for which an engagement quality review is required, including:</p> <ul style="list-style-type: none"> • Determining that an engagement quality reviewer has been appointed; • Cooperating with the engagement quality reviewer and informing other members of the engagement team of their responsibility to do so; • Discussing significant matters and significant judgments arising during the audit engagement, including those identified during the engagement quality review, with the engagement quality reviewer; and • Not dating the auditor’s report until the completion of the engagement quality review. <p>A23. ISAE 3000 (Revised)⁸ also establishes requirements for the engagement partner in relation to the engagement quality review.</p>
<p>(c) Circumstances when the nature and extent of engagement team discussions with the engagement quality reviewer about a significant judgment give rise to a threat to the objectivity of the engagement quality reviewer, and appropriate actions to take in these circumstances. (Ref: Para. A24)</p>	<p><i>Discussions Between the Engagement Quality Reviewer and the Engagement Team</i> (Ref: Para. 21(c))</p> <p>A24. Frequent communication between the engagement team and engagement quality reviewer throughout the engagement may assist in facilitating an effective and timely engagement quality review. However, a threat to the objectivity of the engagement quality reviewer may be created depending on the timing and extent of the discussions with the engagement team about a significant judgment. The firm’s policies or procedures may set forth the actions to be taken by the engagement quality reviewer or the engagement team to avoid situations in which the engagement quality reviewer is, or may be perceived to be, making decisions on behalf of the engagement team. For example, in these circumstances the firm may require consultation about such significant judgments with other relevant personnel in accordance with the firm’s consultation policies or procedures.</p>

⁷ Proposed International Standard on Auditing (ISA) 220 (Revised), *Quality Management for an Audit of Financial Statements*, paragraph 36

⁸ International Standard on Assurance Engagements (ISAE) 3000 (Revised), *Assurance Engagements other than Audits or Reviews of Historical Financial Information*, paragraph 36

ISQM 2 Requirement	Application and Other Explanatory Material
	<i>Procedures Performed by the Engagement Quality Reviewer (Ref: Para. 22–24)</i>
<p>22. In performing the engagement quality review, the engagement quality reviewer shall: (Ref: Para. A25–A28Ax)</p>	<p>A25. The firm’s policies or procedures may specify the nature, timing and extent of the procedures performed by the engagement quality reviewer and also may emphasize the importance of the engagement quality reviewer exercising professional judgment in performing the review.</p> <p>A26. The timing of the procedures performed by the engagement quality reviewer may depend on the nature and circumstances of the engagement, including the nature of the matters subject to the review. Timely review of the engagement documentation by the engagement quality reviewer throughout all stages of the engagement (e.g., planning, risk assessment, performance, completion, reporting) allows matters to be promptly resolved to the engagement quality reviewer’s satisfaction, on or before the date of the engagement report. For example, the engagement quality reviewer may perform procedures in relation to the overall strategy and plan for the engagement at the completion of the planning phase. When the engagement is not complex, and is completed within a short period of time, it may be appropriate for the engagement quality reviewer to perform the procedures near the end of the engagement. Timely performance of the engagement quality review also may reinforce the exercise of professional judgment and, as applicable, professional skepticism, by the engagement team in planning and performing the engagement.</p> <p>A27. The nature and extent of the engagement quality reviewer’s procedures for a specific engagement may depend on, among other factors:</p> <ul style="list-style-type: none"> • The reasons for the assessments given to quality risks, for example, engagements performed for entities in emerging industries or with complex transactions. • Findings arising from the firm’s monitoring activities, and any related guidance issued by the firm, which may indicate areas where more extensive procedures need to be performed by the engagement quality reviewer. • The complexity of the engagement. • The nature and size of the entity, including whether the entity is a listed entity.

ISQM 2 Requirement	Application and Other Explanatory Material
	<ul style="list-style-type: none"> • Other information relevant to the engagement, such as the results of inspections undertaken by an external oversight authority in a prior period, or concerns raised about the commitment to quality of the firm or its personnel. • The firm’s acceptance and continuance of client relationships and specific engagements, which may indicate new risks to achieving quality for an engagement. • For assurance engagements, the engagement team’s consideration of, and responses to, risks of material misstatement in the engagement. • Whether members of the engagement team have cooperated with the engagement quality reviewer. The firm’s policies or procedures may address the actions the engagement quality reviewer takes in circumstances when the engagement team has not cooperated with the engagement quality reviewer, for example, informing an appropriate individual in the firm so appropriate action can be taken to resolve the issue. <p>A28. The nature, timing and extent of the engagement quality reviewer’s procedures may need to change based on circumstances encountered in performing the engagement quality review.</p> <p>Group Audit Considerations</p> <p>A28A. The performance of an engagement quality review for an audit of group financial statements may involve additional considerations for the individual appointed as the engagement quality reviewer for the group audit, depending on the size and complexity of the group. Paragraph 18(a) requires the firm’s policies or procedures to require the engagement quality reviewer to take overall responsibility for the performance of the engagement quality review. In doing so, for larger and more complex group audits, the group engagement quality reviewer may need to discuss significant matters and significant judgments with key members of the engagement team other than the group engagement team (e.g., the partners or other individuals responsible for performing audit procedures on the financial information of a component). In these circumstances, the engagement</p>

ISQM 2 Requirement	Application and Other Explanatory Material
	<p>quality reviewer may be assisted by individuals in accordance with paragraph 17 of this ISQM. The guidance in paragraph A19A may be helpful when the engagement quality reviewer for the group audit is using assistants.</p> <p>A28Ax In some cases, an engagement quality reviewer may be appointed for a component of a group, for example, when required by law, regulation or other reasons. In such circumstances, communication between the engagement quality reviewer for the group audit and the engagement quality reviewer for the component may assist the group engagement quality reviewer in fulfilling the responsibilities in accordance with paragraph 18(a) when significant judgments that relate to the group financial statements were made at the component level.</p>
<p>(a) Read, and obtain an understanding about, information communicated by: (Ref: Para. A28B)</p> <p>(i) The engagement team regarding the nature and circumstances of the entity and the engagement; and</p> <p>(ii) The firm about the results of its monitoring and remediation activities, in particular about identified deficiencies that may relate to, or affect, the areas involving significant judgments by the engagement team.</p>	<p>Information Communicated by the Engagement Team and the Firm (Ref: Para. 22(a))</p> <p>A28B. Obtaining an understanding about information communicated by the engagement team and the firm in accordance with paragraph 22(a) of this ISQM may assist the engagement quality reviewer in understanding the significant judgments that may be expected for the engagement. Such an understanding may also provide the engagement quality reviewer with a basis for discussions with the engagement team about the significant matters and significant judgments made in planning, performing, concluding and reporting on the engagement.</p>
<p>(b) Discuss with the engagement partner and, if applicable, other members of the engagement team, significant matters and significant judgments made in planning, performing,</p>	<p>Significant Matters and Significant Judgments (Ref: Para. 22(b)–22(c))</p> <p>A29. For audits of financial statements, proposed ISA 220 (Revised)⁹ requires the engagement partner to review audit documentation relating to significant matters¹⁰ and</p>

⁹ Proposed ISA 220 (Revised), paragraph 31

¹⁰ ISA 230, *Audit Documentation*, paragraph 8(c)

ISQM 2 Requirement	Application and Other Explanatory Material
<p>concluding and reporting on the engagement. (Ref: Para. A29–A31A)</p>	<p>significant judgments, including those relating to difficult or contentious matters identified during the course of the engagement, and the conclusions reached.</p> <p>A30. For audits of financial statements, proposed ISA 220 (Revised)¹¹ provides examples of significant judgments that may be identified by the engagement partner related to the overall audit strategy and audit plan for undertaking the engagement, the execution of the engagement and the overall conclusions reached by the engagement team.</p> <p>A31. For engagements other than audits of financial statements, the significant judgments made by the engagement team may depend on the nature and circumstances of the engagement. For example, in an assurance engagement performed in accordance with ISAE 3000 (Revised), the engagement team’s determination of whether the criteria to be applied in the preparation of the subject matter information are suitable for the engagement may involve or require significant judgment.</p> <p>A31A. In performing the engagement quality review, the engagement quality reviewer may become aware of other areas where significant judgments would have been expected to be made by the engagement team for which further information may be needed about the engagement team’s procedures or conclusions. In those circumstances, discussions with the engagement quality reviewer may result in the engagement team concluding that additional procedures need to be performed.</p>
<p>(c) Based on the information obtained in (a) and (b), review selected engagement documentation relating to the significant judgments made by the engagement team and evaluate: (Ref: Para. A31Ax–A31Cb)</p> <p>(i) The basis for making those significant judgments, including, when applicable to the type of engagement, the exercise of</p>	<p>A31Ax. In evaluating the engagement team’s basis for making significant judgments, including, when applicable to the type of engagement, the exercise of professional skepticism, the engagement quality reviewer may:</p> <ul style="list-style-type: none"> • Remain alert to changes in the nature and circumstances of the engagement or the entity that may result in changes in the significant judgments made by the engagement team; • Apply an unbiased view in evaluating responses from the engagement team; and

¹¹ Proposed ISA 220 (Revised), paragraph A88

ISQM 2 Requirement	Application and Other Explanatory Material
<p>professional skepticism by the engagement team;</p> <p>(ii) Whether the engagement documentation supports the conclusions reached; and</p> <p>(iii) Whether the conclusions reached are appropriate.</p>	<ul style="list-style-type: none"> • Follow-up on inconsistencies identified in reviewing engagement documentation, or inconsistent responses by the engagement team to questions relating to the significant judgments made. <p>A31B. The firm’s policies or procedures may specify engagement documentation to be reviewed by the engagement quality reviewer. In addition, such policies or procedures may indicate that the engagement quality reviewer exercises professional judgment in selecting additional engagement documentation to be reviewed relating to significant judgments made by the engagement team.</p> <p>A31C. Discussions about significant judgments with the engagement partner, and if applicable, other members of the engagement team, and the engagement team’s documentation, may assist the engagement quality reviewer in evaluating the exercise of professional skepticism by the engagement team in relation to those significant judgments.</p> <p>A31Ca. Requirements and relevant application material in ISA 315 (Revised 2019),¹² ISA 540 (Revised)¹³ and other ISAs provide examples of ways in which the auditor can exercise professional skepticism, or ways in which documentation may provide evidence of the auditor’s exercise of professional skepticism. Such guidance may also assist the engagement quality reviewer in evaluating the exercise of professional skepticism by the engagement team.</p> <p>A31Cb. Proposed ISA 220 (Revised)¹⁴ provides examples of the impediments to the exercise of professional skepticism at the engagement level, unconscious auditor biases that may impede the exercise of professional skepticism, and possible actions that the engagement team may take to mitigate impediments to the exercise of professional skepticism at the engagement level.</p>

¹² ISA 315 (Revised 2019), *Identifying and Assessing the Risks of Material Misstatement*, paragraph A238

¹³ ISA 540 (Revised), *Auditing Accounting Estimates and Related Disclosures*, paragraph A11

¹⁴ Proposed ISA 220 (Revised), paragraphs A35-A37

ISQM 2 Requirement	Application and Other Explanatory Material
<p>(d) For audits of financial statements, evaluate the basis for the engagement partner’s determination that relevant ethical requirements relating to independence have been fulfilled. (Ref: Para. A31D)</p>	<p>Whether Relevant Ethical Requirements Relating to Independence Have Been Fulfilled (Ref: Para. 22(d))</p> <p>A31D. Proposed ISA 220 (Revised)¹⁵ requires that, prior to dating the auditor’s report, the engagement partner shall take responsibility for determining whether relevant ethical requirements, including those related to independence, have been fulfilled.</p>
<p>(e) Evaluate whether appropriate consultation has taken place on difficult or contentious matters or matters involving differences of opinion and the conclusions arising from those consultations. (Ref: Para. A32)</p>	<p>Whether Consultation Has Taken Place on Difficult or Contentious Matters or Matters Involving Differences of Opinion (Ref: Para. 22(e))</p> <p>A32. The firm may establish policies or procedures that address consultation on difficult or contentious matters and differences of opinion within the engagement team, or between the engagement team and the engagement quality reviewer.</p>
<p>(f) For audits of financial statements, evaluate whether the engagement partner’s involvement has been sufficient and appropriate throughout the audit engagement such that the engagement partner has the basis for determining that the significant judgments made and the conclusions reached are appropriate given the nature and circumstances of the engagement. (Ref: Para. A33)</p>	<p>Sufficient and Appropriate Involvement of the Engagement Partner on the Engagement (Ref: Para. 22(f))</p> <p>A33. Proposed ISA 220 (Revised)¹⁶ requires the engagement partner to determine, prior to dating the auditor’s report, that the engagement partner’s involvement has been sufficient and appropriate throughout the audit engagement such that the engagement partner has the basis for determining that the significant judgments made and the conclusions reached are appropriate given the nature and circumstances of the engagement. Proposed ISA 220 (Revised)¹⁷ also indicates that the documentation of the involvement of the engagement partner may be accomplished in different ways. Discussions with the engagement team, and review of such engagement documentation, may assist the engagement quality reviewer’s evaluation of the sufficiency and appropriateness of the engagement partner’s involvement.</p>

¹⁵ Proposed ISA 220 (Revised), paragraph 21

¹⁶ Proposed ISA 220 (Revised), paragraph 40(a)

¹⁷ Proposed ISA 220 (Revised), paragraph A114

ISQM 2 Requirement	Application and Other Explanatory Material
<p>(g) Review:</p> <p>(i) For an audit of financial statements, the financial statements and the auditor's report thereon, including, if applicable, the description of the key audit matters; or (Ref: Para. A33B)</p> <p>(ii) For an assurance or related services engagement, the engagement report, and when applicable, the subject matter information. (Ref: Para. A33C)</p>	<p>Review of Financial Statements and Engagement Reports (Ref: Para. 22(g))</p> <p>A33B. For audits of financial statements, the engagement quality reviewer's review of the financial statements and auditor's report thereon may include consideration of whether the presentation and disclosure of matters relating to the significant judgments made by the engagement team are consistent with the engagement quality reviewer's understanding of those matters based on the review of selected engagement documentation, and discussions with the engagement team. In reviewing the financial statements, the engagement quality reviewer may also become aware of other areas where significant judgments would have been expected to be made by the engagement team for which further information may be needed about the engagement team's procedures or conclusions.</p> <p>A33C. For assurance or related services engagements, the engagement quality reviewer's review of the engagement report and, when applicable, the subject matter information may include considerations similar to those described in paragraph A33B (e.g., whether the presentation or description of matters relating to the significant judgments made by the engagement team are consistent with the engagement quality reviewer's understanding based on the procedures performed in connection with the review).</p>
	<p>Unresolved Concerns of the Engagement Quality Reviewer (Ref: Para. 23)</p>
<p>23. The engagement quality reviewer shall notify the engagement partner if the engagement quality reviewer has concerns that the significant judgments made by the engagement team, or the conclusions reached thereon, are not appropriate. If such concerns are not resolved to the engagement quality reviewer's satisfaction, the engagement quality reviewer shall notify an appropriate individual(s) in the firm that the engagement quality review cannot be completed. (Ref: Para. A35)</p>	<p>A35. The firm's policies or procedures may specify the individual(s) in the firm to be notified if the engagement quality reviewer has unresolved concerns that the significant judgments made by the engagement team, or the conclusions reached thereon, are not appropriate. Such individual(s) may include the individual assigned the responsibility for the appointment of engagement quality reviewers. With respect to such unresolved concerns, the firm's policies or procedures may also require consultation within or outside the firm (e.g., a professional or regulatory body).</p>

ISQM 2 Requirement	Application and Other Explanatory Material
<i>Completion of the Engagement Quality Review</i>	
24. The engagement quality reviewer shall determine whether the requirements in this ISQM with respect to the performance of the engagement quality review have been fulfilled, and whether the engagement quality review is complete. If so, the engagement quality reviewer shall notify the engagement partner that the engagement quality review is complete.	
Documentation	Documentation (Ref: Para. 25–27)
25. The firm shall establish policies or procedures that require the engagement quality reviewer to take responsibility for documentation of the engagement quality review. (Ref: Para. A36)	A36. Paragraphs 66 to 69 of proposed ISQM 1 require the firm to prepare documentation of the firm’s system of quality management. An engagement quality review performed in accordance with this ISQM is a specified response to assessed quality risks related to the performance of engagements, and is therefore subject to those documentation requirements in proposed ISQM 1.
26. The firm shall establish policies or procedures that require documentation of the engagement quality review in accordance with paragraph 27, and that such documentation be included with the engagement documentation.	
27. The engagement quality reviewer shall determine that the documentation of the engagement quality review is sufficient to enable an experienced practitioner, having no previous connection with the engagement, to understand the nature, timing and extent of the procedures performed by the engagement quality reviewer and, when applicable, individuals who assisted the reviewer, and the conclusions reached in performing	A37. The form, content and extent of the documentation of the engagement quality review may depend on factors such as: <ul style="list-style-type: none"> • The nature and complexity of the engagement; • The nature of the entity; • The nature and complexity of the matters subject to the engagement quality review; and

ISQM 2 Requirement	Application and Other Explanatory Material
<p>the review. The engagement quality reviewer also shall determine that the documentation of the engagement quality review includes: (Ref: Para. A37–A39)</p> <ul style="list-style-type: none"> (a) The names of the engagement quality reviewer and individuals who assisted with the engagement quality review; (b) An identification of the engagement documentation reviewed; (c) The basis for the engagement quality reviewer's determination in accordance with paragraph 24; (d) The notifications required in accordance with paragraphs 23 and 24; and (e) The date of completion of the engagement quality review. 	<ul style="list-style-type: none"> • The extent of the engagement documentation reviewed. <p>A38. The performance and notification of the completion of the engagement quality review may be documented in a number of ways. For example, the engagement quality reviewer may document the review of engagement documentation electronically in the IT application for the performance of the engagement. Alternatively, the engagement quality reviewer may document the review through means of a memorandum. The engagement quality reviewer's procedures may also be documented as part of the engagement documentation, for example, minutes of the engagement team's discussions where the engagement quality reviewer was present.</p> <p>A39. Paragraph 21(b) of this ISQM requires that the firm's policies or procedures preclude the engagement partner from dating the engagement report until the completion of the engagement quality review, which includes resolving matters raised by the engagement quality reviewer. Provided that all requirements with respect to the performance of the engagement quality review have been fulfilled, the documentation of the review may be finalized after the date of the engagement report, but before the assembly of the final engagement file. However, firm policies or procedures may specify that the documentation of the engagement quality review needs to be finalized on or before the date of the engagement report.</p>



AUASB Board Meeting Summary Paper

AGENDA ITEM NO. **5.0**

Meeting Date: 3 March 2020

Subject: Proposed ISA 220 Quality Management for an Audit of Financial Statements

Prepared By: Tim Austin

Date Prepared: 2 March 2020

Action Required

For Information Purposes Only

A. Background

- 1 At the September and December 2019 IAASB Meetings, the ISA 220 Task Force completed their review of comments received, presented their recommendations to respond to comments and completed redrafting of the standard relating to:
 - (a) Engagement Partner's role and overall responsibility;
 - (b) Engagement Team definition;
 - (c) Scalability;
 - (d) Direction, supervision and review;
 - (e) Ability to depend on the firm's system;
 - (f) Public interest matters;
 - (g) Objective of the standard;
 - (h) Professional scepticism;
 - (i) Stand-back provision;
 - (j) Technology; and
 - (k) Documentation.
- 2 For the March 2020 IAASB Meeting, the ISA 220 Taskforce considers that it has responded to all feedback from submissions to the ED and feedback from IAASB Members and will be asking for IAASB Members to indicate their support for the redrafted ISA 220 with the intention of approving the standard at the June 2020 IAASB Meeting.

This document contains preliminary views and/or AUASB Technical Group recommendations to be considered at a meeting of the AUASB, and does not necessarily reflect the final decisions of the AUASB. No responsibility is taken for the results of actions or omissions to act on the basis of reliance on any information contained in this document (including any attachments), or for any errors or omissions in it.

B. What the Audit Technical Group (ATG) is seeking from the AUASB at the December 2019 AUASB meeting

3 The objectives of this agenda item are to:

- (a) update the AUASB on the key changes to proposed ISA 220 since the December 2020 IAASB Meeting; and
- (b) For the AUASB to provide comments on the key areas highlighted by the AUASB Technical Group to provide to the AUASB Chair in their capacity as an IAASB member.

4 The ATG has carried forward and updated the analysis of whether the proposed changes appropriately address that matters raised by the AUASB in its submission on ED-220, as well as matters raised by the AUASB at the September and December AUASB Meetings.

5 Based on the IAASB's Paper, this is likely to be the last opportunity for AUASB Members to raise significant issues with the standard. Relevant sections of the standard have been extracted and included in this paper to allow AUASB Members provide detailed responses to questions 1 to 5.

6 The ATG draws the AUASB's attention to the fact that the standard is unlikely to change significantly before voting and this will be the last opportunity to raise significant concerns. A clean copy of the full standard has been provided as Agenda Item 5.1.

C. Changes since the December IAASB Meeting:

7 At the December 2019 AUASB Meeting, the ATG provided AUASB Members with a summary of the key changes to the standard and asked for comments on the changes. These areas included:

- (a) The engagement team definition;
- (b) Delegating and assigning;
- (c) Direction, supervision and review; and
- (d) Reliance on the firm's systems.

8 The IAASB at the December 2019 IAASB Meeting made a number of comments to the Task Force on their proposed way forward for these areas. This section of the Paper will summarise the Task Force's responses to the feedback.

E.1 Engagement Team Definition

9 For the December 2019 IAASB Meeting, the Task Force made a number of changes to the engagement team definition including:

- (a) Explaining what is meant by "audit procedures" through a new paragraph, A17;
- (b) Clarifying in a new paragraph, A18, that the engagement team definition includes other auditors who perform audit procedures; and
- (c) Clarifying, through amendments to paragraph A20, that an individual with expertise whose involvement in the engagement is limited to consultation is not a member of the engagement team.

10 The AUASB considered that the engagement team definition was improved by the changes, in particular, clarifying what is meant by audit procedures. However, the AUASB still raised that the interaction between the expanded engagement team definition and the requirements was still a concern. There have been limited changes to the definition since the December 2019 IAASB Meeting.

E.2 Engagement Partner’s Role and Overall Responsibility including Direction, Supervision and Review

- 11 The AUASB over the course of the development of ISA 220 have raised a number of concerns with the drafting of the Engagement Partner’s responsibilities and whether they could be practically met by the engagement partner. Since ED-220 was exposed, there has been a significant amount of redrafting by the IAASB Task Force. The ATG draws the AUASB’s attention to the following key areas of the engagement partner’s responsibilities for consideration:
- (a) The IAASB’s proposed approach to indicate paragraphs that must be performed by the engagement partner and those that can be delegated to other members of the engagement team;
 - (b) Proposed changes to the paragraph on assigning requirements; and
 - (c) The ability to rely on the firm’s systems.

Engagement Partner Responsibilities

- 12 Throughout the development of the standard, AUASB Members have raised that it may be difficult for the engagement partner to practically meet the requirements, particularly in engagements whose nature and circumstances are more complex as well as the expanded engagement team.
- 13 In response to this, at the December 2019 IAASB Meeting, the Taskforce proposed introducing a lead in to paragraphs to indicate whether they may be assigned or must be completed by the engagement partner. The Taskforce has landed on the wording:
- (a) Requirements that are the engagement partner’s sole responsibility – *“the engagement partner shall”*.
 - (b) Requirements for which the engagement partner is permitted to assign – *“the engagement partner shall take responsibility for”*.
- 14 When last discussed, the ATG raised that the communication of this approach in the standard was not sufficiently clear and that it is important that the approach is clear to all stakeholders without digging through application material or other explanatory material (particularly in Australia where the standards have force-of-law). In response to this, the IAASB has moved paragraph A29A to the Introduction as paragraphs 8 and 9.

ISA 220

Paragraph 8

The requirements of this ISA are intended to be applied in the context of the nature and circumstances of each audit. For example:

- a) When an audit is carried out entirely by the engagement partner, which may be the case for an audit of a less complex entity, some requirements in this ISA are not relevant because they are conditional on the involvement of other members of the engagement team. (Ref: Para. A14–A15)
- b) In an audit of an entity whose nature and circumstances are more complex, the engagement partner may assign the design or performance of some procedures, tasks or actions to other members of the engagement team.

Paragraph 9

When this ISA expressly intends that a requirement or responsibility be fulfilled by the engagement partner, the term *“the engagement partner shall ...”* is used. In such circumstances, the engagement partner may need

to obtain information from the firm or other members of the engagement team to fulfil the requirement. For example, the engagement partner may need to gather information from engagement team members about suspected breaches of relevant ethical requirements in accordance with paragraph 19. When the engagement partner is permitted to assign the design or performance of procedures, tasks or actions to appropriately skilled or suitably experienced members of the engagement team, the term “the engagement partner shall take responsibility for...” is used. Nevertheless, the engagement partner remains ultimately responsible, and therefore accountable, for compliance with the requirements of this ISA. (Ref: Para. A23–A25)

- 15 Whilst the ATG supports moving the explanation from application and explanatory material to the introduction of the standard, the ATG considers it important for the IAASB to outline, for each requirement, how they have determined that the requirement may or may not be delegated to other members of the engagement team. Having a clear rationale will assist with developing implementation guidance for the standard including additional examples.

Questions

1. Do AUASB Members consider that proposed paragraphs 8 and 9 sufficiently describe to readers how to identify requirements which are solely the responsibility of the engagement partner and those which can be delegated to other members of the engagement team?
2. Do AUASB Members consider it important to raise with the IAASB that a clear rationale for why a requirement may or may not be delegated to another member of the engagement team should be provided with the standard?

Assigning Procedures

- 16 The AUASB in its submission raised that the requirements on direction, supervision and review on their own did not appear overly onerous but became onerous when considering the broad engagement team definition and the impracticality with expecting an individual engagement partner to perform all the requirements.
- 17 In responding to this at an IAASB level, the Task Force was directed to consider in the direction, supervision and review section of the standard:
- (a) Clarifying the nature, timing and extent of direction, supervision and review in more complex engagements, including differences between what is required for individuals outside of the firm’s network.
 - (b) Clarifying that areas requiring increased professional judgement also require increased partner involvement.
- 18 The Taskforce responded to the feedback from the IAASB by introducing three new paragraphs in the application material to the proposed standard as well as clarifying in the standard requirements that may be assigned to other members.
- 19 A further change has been made by the Task Force to the paragraph addressing assigning of procedures to other engagement team members to clarify that whilst the engagement partner needs to continue to take overall responsibility for the engagement, the engagement partner directs, supervises and reviews the work of engagement team members to which the engagement partner **assigned work**.

- 20 The ATG considers that this addresses the AUASB’s concern that the requirements of the standard become significantly onerous in conjunction with the expanded engagement team.

ISA 220, paragraph 15

If the engagement partner assigns the design or performance of procedures, tasks or actions related to a requirement of this ISA to other members of the engagement team to assist the engagement partner in complying with the requirements of this ISA, the engagement partner shall continue to take overall responsibility for managing and achieving quality on the audit engagement through direction and supervision of those members of the engagement team, and review of their work, ~~as required by paragraph 27.~~ (Ref: Para. ~~A29A A309, A38~~)

Questions

3. Do AUASB Members agree with the proposed changes to paragraph 15 to clarify direction, supervision and review to members of the engagement team to which the engagement partner assigned work?

Ability to Rely on the Firm’s Systems

- 21 The IAASB agreed with the respondents who asked for clarity regarding what the engagement partner needs to do to depend on the firm’s system of quality management and made amendments to the application material in the standard to clarify that “*ordinarily, the engagement partner may depend on the firm’s system of quality management, except when...*”
- 22 The AUASB raised in its submission that the removal of the explicit statement from the introduction of the extant standard that “*Engagement teams are entitled to rely on the firm’s system of quality control...*” and the proposed approach of using “*shall be satisfied*” and “*shall determine*” to differentiate between actions that can occur at a firm level and actions that must occur at an engagement level created difficulties in meeting the requirements of the proposed standard. These terms are still used throughout the proposed standard.
- 23 The ATG considered that the IAASB’s amendments to the application material do not respond appropriately to the AUASB’s concerns. The ATG views that there should be material in the requirements which outlines that the objective of the standard is to obtain reasonable assurance that quality has been achieved and in some situations evidence provided by the firm is better than the evidence that the individual engagement partner could obtain (e.g. does anybody on the engagement team hold shares in the audited entity).
- 24 The ATG still considers that the paragraph in the Introduction does not sufficiently outline the situations where an engagement team can rely on the firm’s systems, including articulating what is required of an engagement partner where they choose to rely on those firm systems.

Questions

4. Do AUASB Members agree with the ATG’s view in paragraph 24 that material regarding the engagement partner’s ability to rely on the firm’s system is still not clear?

E.3 Other Matters

- 25 The AUASB raised at the December 2019 AUASB Meeting that the conforming amendment to ISA 300 requiring the Audit Plan to include a description of the nature, timing and extent of the direction and supervision of the engagement team members and the review of their work would not drive appropriate behaviour and would result in a checklist approach.
- 26 Additionally, the conforming amendment to paragraph 11 of ISA 300 requiring the engagement partner to review the audit strategy and audit plan was not appropriate in a larger audit environment with component auditors. The audit strategy should be reviewed but not the audit plan, it is too granular to provide value.

Questions

5. Do AUASB Members consider that the AUASB Chair should raise as part of ISA 600 that the requirement to review the audit plan is still inappropriate?

D. The way forward:

- 27 The Task Force is working towards approving the standard at the June 2020 IAASB Meeting and that the meeting will only cover matters related to coordination with other projects.
- 28 The AUASB Technical Group will perform a review of changes made to the proposed standard following the March 2020 IAASB Meeting and advise AUASB members of any additional significant changes. Further analysis will be performed in conjunction with our review of the papers for the June 2020 IAASB Meeting.



AUASB Submission and IAASB Response

Matter #	Point raised by AUASB	Where in AUASB's submission	Has this been considered by the IAASB?
1	<p>Monitoring and reviewing work of assignees</p> <p>The AUASB considers that it may be difficult to practically meet the requirements in paragraphs 11-13 on a larger audit engagement (such as a multinational or group audit), particularly allowing for the broader Engagement Team definition now contained in the proposed standard. The AUASB specifically draws attention to the requirement in paragraph 13(b) outlining the engagement partner's responsibility to monitor and review the work of assignees, which we consider may be difficult to achieve with this expanded engagement team definition in place.</p>	Qn. 1	<p>Yes – Points raised have been considered by the IAASB.</p> <p>Response from the Task Force has included proposed changes to:</p> <ul style="list-style-type: none">- clarify who is in and out of the engagement team;- changes to paragraph 15 to outline that the engagement partner takes overall responsibility for direction, supervision and review but directs, supervises and reviews the work of team members who they assigned work to;- clarifying the nature, timing and extent of direction, supervision and review in more complex engagements, including differences between what is required for individuals outside of the firm's network;- planned implementation guidance to address "upwards" scalability.
2	<p>Guidance Direction and Supervision</p> <p>The AUASB considers that whilst the direction, supervision and review requirements on their own do not appear overly onerous, they may not be practically achievable as a result of the broader engagement team definition. The AUASB is concerned that the broad definition of engagement team may draw in unintended personnel into the engagement team.</p>	Qn. 5	<p>Yes – Points raised have been considered by the IAASB.</p> <p>Response from the Task Force has included proposed changes to:</p> <ul style="list-style-type: none">- clarify who is in and out of the engagement team;- changes to paragraph 15 to outline that the engagement partner takes overall responsibility for direction, supervision and review but directs, supervises and reviews the work of team members who they assigned work to; and- more clearly identify requirements which must be performed by the engagement partner and those that can be assigned.

This document contains preliminary views and/or AUASB Technical Group recommendations to be considered at a meeting of the AUASB, and does not necessarily reflect the final decisions of the AUASB. No responsibility is taken for the results of actions or omissions to act on the basis of reliance on any information contained in this document (including any attachments), or for any errors or omissions in it.

Matter #	Point raised by AUASB	Where in AUASB's submission	Has this been considered by the IAASB?
3	<p>Ambiguity of definitions across the QM suite in relation to Engagement Team</p> <p>... the AUASB raises a significant concern that the definition of engagement team may be interpreted differently under ISA 220 and ISQM 1 due to the different application and explanatory material that applies to this definition in ISA 220 (paragraphs A16-A19) not being replicated in ISQM 1.</p>	Qn. 2	<p>Yes – The ISQM 1 Task Force has indicated in the March 2020 papers that the definition will be aligned to ISA 220. .</p>
4	<p>Engagement Partner's role</p> <p>With regard to the roles of other senior members, including other partners, the AUASB would like the IAASB to provide further guidance dealing with situation where there are multiple partners on an engagement. Whilst Australian stakeholders did not view this as a significant issue with the proposed standard, the AUASB considers that with global actions in response to audit quality, such as proposals for more than one audit firm to perform an engagement, the need for clarification will arise in the future and should be addressed now to avoid reopening the standard.</p> <p>The AUASB recommends that the IAASB considers the impact of new and emerging technology on all aspects of the engagement partner's responsibilities and is not limited to engagement resources. In the absence of appropriate technology considerations within the standard, additional implementation and guidance materials may be required to support practitioners to understand how an engagement partner can meet the requirements of the standards in a modern environment.</p>	Qn. 1 & Qn. 4	<p>No – The Task Force has not included the signing partner project as part of the papers at either September or December.</p> <p>Yes – The Task Force considers that the standard appropriately deals with technology and that the Task Force will work with the AEWG and TWG to develop implementation guidance.</p>
5	<p>Definitions</p> <p>The AUASB considers that whilst the direction, supervision and review requirements on their own do not appear overly</p>	Qn. 5	<p>Yes – Points raised have been considered by the IAASB.</p> <p>Response from the Task Force has included proposed changes to:</p> <ul style="list-style-type: none"> - clarify who is in and out of the engagement team;

This document contains preliminary views and/or AUASB Technical Group recommendations to be considered at a meeting of the AUASB, and does not necessarily reflect the final decisions of the AUASB. No responsibility is taken for the results of actions or omissions to act on the basis of reliance on any information contained in this document (including any attachments), or for any errors or omissions in it.

Matter #	Point raised by AUASB	Where in AUASB's submission	Has this been considered by the IAASB?
	onerous, they may not be practically achievable as a result of the broader engagement team definition. The AUASB is concerned that the broad definition of engagement team may draw in unintended personnel into the engagement team.		<ul style="list-style-type: none"> - additional application material clarifying what is an “audit procedure”; and - component auditors are part of the engagement team.
6	<p>How do the changes improve audit quality?</p> <p>The AUASB recommends that the IAASB considers the impact of new and emerging technology on all aspects of the engagement partner’s responsibilities and is not limited to engagement resources. In the absence of appropriate technology considerations within the standard, additional implementation and guidance materials may be required to support practitioners to understand how an engagement partner can meet the requirements of the standards in a modern environment.</p>	Qn. 4	Yes – The Task Force considers that the standard appropriately deals with technology and that the Task Force will work with the AEWG and TWG to develop implementation guidance.
7 & 8	<p>Requirements and Reliance on Firm’s System</p> <p>Overall, the ability to practically meet the direction, supervision and review requirements of the proposed standard is further impacted by removal of paragraph 4 from the extant ISA 220 which stated “Engagement teams are entitled to rely on the firm’s system of quality control process, unless information provided by the firm or other parties suggests otherwise”. The IAASB’s proposed approach of using the terms “shall be satisfied” and “shall determine” to differentiate between actions that can occur at a firm level and actions that must occur at an engagement level is not clearly articulated in the body of ISA 220 and is not commonly used throughout the suite of auditing standards which may result in diverse interpretation.</p>	Qn.5	Yes – IAASB agreed with the respondents who asked for clarity regarding what the engagement partner needs to do to depend on the firm’s system of quality management. Task Force has amended relevant application material to consider this.
9	Roles of EP and EQR	Qn. 2	No – The Task Force has not included this as part of the papers at either September or December.

This document contains preliminary views and/or AUASB Technical Group recommendations to be considered at a meeting of the AUASB, and does not necessarily reflect the final decisions of the AUASB. No responsibility is taken for the results of actions or omissions to act on the basis of reliance on any information contained in this document (including any attachments), or for any errors or omissions in it.

Matter #	Point raised by AUASB	Where in AUASB's submission	Has this been considered by the IAASB?
	<p>The AUASB also raises for consideration whether an appropriate balance has been achieved between the role of the engagement partner under ISA 220 and the role of the EQR under ISQM 2. In particular, the AUASB draws attention to paragraph 22(c) of ISQM 2 where the EQR is required to “identify” areas involving significant judgments rather than “evaluate” the areas identified by the engagement team; and paragraph 22(f) where the EQR is required to evaluate the Engagement Partner’s (EP) stand-back requirement. The level of work expected of the EQR in some areas appears to be at the same level as an EP and, in the view of the AUASB, is not in line with the objectives and proportionate responsibilities of an EQR.</p>		
10	<p>Documentation</p> <p>The AUASB generally views that the documentation requirements in conjunction with the requirements of ISA 230 provide sufficient guidance on documentation although this can be enhanced by a link between the review requirements of the engagement partner and the documentation requirements to evidence this review.</p>	Qn. 6	<p>Yes – The Task Force has made amendments to clarify documentation requirements including the addition of a conforming amendment to ISA 300 to outline that documentation of the audit plan can include description of the nature, timing and extent of the direction and supervision of the engagement team members and the review of their work.</p>
11	<p>Review of Technology</p> <p>The AUASB considers that the standard does not adequately deal with advances in technology and potential changes in the auditing environment. For example, as the use of Artificial Intelligence/machine learning becomes more common, it is unclear how the review requirements of the standard will be met, particularly where specialist knowledge is required to review such tools.</p>	Qn. 4	<p>Yes – The Task Force considers that the standard appropriately deals with technology and that the Task Force will work with the AEWG and TWG to develop implementation guidance.</p>
12	<p>Scalability – Network Reliance</p>	Qn. 7	<p>Yes – IAASB agreed with the respondents who asked for clarity regarding what the engagement partner needs to do to depend on</p>

This document contains preliminary views and/or AUASB Technical Group recommendations to be considered at a meeting of the AUASB, and does not necessarily reflect the final decisions of the AUASB. No responsibility is taken for the results of actions or omissions to act on the basis of reliance on any information contained in this document (including any attachments), or for any errors or omissions in it.

Matter #	Point raised by AUASB	Where in AUASB's submission	Has this been considered by the IAASB?
	<p>Australian stakeholders raised that the removal of paragraph 4 from the extant ISA 220 which stated "Engagement teams are entitled to rely on the firm's system of quality control process, unless information provided by the firm or other parties suggests otherwise" and changes to the standard to explicitly state that the firm's system of quality control cannot be relied upon in certain situations may impact on scalability. Stakeholders viewed that the benefits of being part of a network may be lost, therefore placing more onus on individual firms and partners impacting scalability.</p>		<p>the firm's system of quality management. Task Force has amended relevant application material to consider this.</p>
<p>13</p>	<p>Professional Skepticism</p> <p>The AUASB views that the objective of paragraph 7 is unclear. Presently, the requirement may appear to lead engagement team members to question or 'second guess' their colleagues and/or the firm in meeting the requirements of this standard. The AUASB questions whether this was the intention of this revision to the proposed standard and considers that paragraph 7, and other appropriate areas of ISA 220, should more clearly emphasise how the engagement partner is responsible for establishing an environment that supports the exercise of professional scepticism and setting an appropriate 'tone from the top' across the engagement team.</p>	<p>Qn. 3</p>	<p>Yes – The Task Force has reconsidered the application material to paragraph 7. This has resulted in:</p> <ul style="list-style-type: none"> - no substantial changes to paragraph 7; - significant redrafting of paragraph A27, although no new impediments to skepticism included; and - future consideration by the Task Force of examples to be included as part of implementation material for the standard.

This document contains preliminary views and/or AUASB Technical Group recommendations to be considered at a meeting of the AUASB, and does not necessarily reflect the final decisions of the AUASB. No responsibility is taken for the results of actions or omissions to act on the basis of reliance on any information contained in this document (including any attachments), or for any errors or omissions in it.

Agenda Item 2-B

[Proposed] International Standard on Auditing (ISA) 220 (Revised), *Quality Management for an Audit of Financial Statements*

Note for IAASB

Words highlighted in grey are subject to change from proposed ISQM 1,¹ proposed ISQM 2² or proposed ED-600.³

At the December 2019 IAASB meeting, limited changes were proposed to the paragraphs in grey to respond to issues raised by respondents to the exposure draft and to align with the latest text of other standards. To avoid misalignment while these standards are still being developed, these paragraphs have reverted back to the ED-220⁴ wording, except when necessary to respond to comments on ED-220. As noted in **Agenda Item 2**, the Task Force will fully align these paragraphs in Q2 of 2020.

Introduction

Scope of this ISA

1. This International Standard on Auditing (ISA) deals with the specific responsibilities of the auditor regarding quality management at the engagement level for an audit of financial statements, and the related responsibilities of the engagement partner. This ISA is to be read in conjunction with relevant ethical requirements. (Ref: Para. A1–A2)

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

2. The firm is responsible for the system of quality management. Under [proposed] ISQM 1, the objective of the firm is to design, implement and operate a system of quality management for audits and reviews of financial statements, and other assurance and related services engagements performed by the firm, that provides the firm with reasonable assurance that: (Ref: Para. A14–A15)
 - (a) The firm and its personnel fulfill their responsibilities in accordance with professional standards and applicable legal and regulatory requirements, and conduct engagements in accordance with such standards and requirements; and
 - (b) Engagement reports issued by the firm or engagement partners are appropriate in the circumstances.⁵
3. This ISA is premised on the basis that the firm is subject to the ISQMs or to national requirements that are at least as demanding. (Ref: Para. A3–A4)

¹ Proposed International Standard on Quality Management (ISQM) 1, *Quality Management for Firms that Perform Audits or Reviews of Financial Statements, or Other Assurance or Related Services Engagements*

² Proposed ISQM 2, *Engagement Quality Reviews*

³ Proposed ISA 600, *Special Considerations—Audits of Group Financial Statements (Including the Work of Component Auditors)*

⁴ Proposed ISA 220 (Revised), *Quality Management for an Audit of Financial Statements*

⁵ Proposed ISQM 1, paragraph 21

4. The engagement team, led by the engagement partner, is responsible, within the context of the firm's system of quality management and through complying with the requirements of this ISA, for:
 - (a) Implementing the firm's responses to quality risks (i.e., the firm's policies or procedures) that are applicable to the audit engagement using information communicated by, or obtained from, the firm; (Ref: Para. A5–A7)
 - (b) Given the nature and circumstances of the audit engagement, determining whether to design and implement responses at the engagement level beyond those set forth in the firm's policies or procedures; and (Ref: Para. A8–A10)
 - (c) Providing the firm with information from the audit engagement required to be communicated by the firm's policies or procedures to support the design, implementation and operation of the firm's system of quality management. (Ref: Para. A11–A12)
5. Complying with the requirements in other ISAs may provide information that is relevant to quality management at the engagement level. (Ref: Para. A13)
6. The public interest is served by the consistent performance of quality audit engagements through achieving the objective of this standard and other ISAs for each engagement. A quality audit engagement is achieved through planning and performing the engagement and reporting on it in accordance with professional standards and applicable legal and regulatory requirements. Achieving the objectives of professional standards and complying with the requirements of applicable law or regulation involves exercising professional judgment and exercising professional skepticism.
7. In accordance with ISA 200,⁶ the engagement team is required to plan and perform an audit with professional skepticism and to exercise professional judgment. Professional judgment is exercised in making informed decisions about the courses of action that are appropriate to manage and achieve quality given the nature and circumstances of the audit engagement. Professional skepticism supports the quality of judgments made by the engagement team and, through these judgments, supports the overall effectiveness of the engagement team in achieving quality at the engagement level. The appropriate exercise of professional skepticism may be demonstrated through the actions and communications of the engagement team. Such actions and communications may include specific steps to mitigate impediments that may impair the appropriate exercise of professional skepticism, such as unconscious bias or resource constraints. (Ref: Para. A34–A37)
8. The requirements of this ISA are intended to be applied in the context of the nature and circumstances of each audit. For example:
 - (a) When an audit is carried out entirely by the engagement partner, which may be the case for an audit of a less complex entity, some requirements in this ISA are not relevant because they are conditional on the involvement of other members of the engagement team. (Ref: Para. A14–A15)
 - (b) In an audit of an entity whose nature and circumstances are more complex, the engagement partner may assign the design or performance of some procedures, tasks or actions to other members of the engagement team.

⁶ ISA 200, *Overall Objectives of the Independent Auditor and the Conduct of an Audit in Accordance with International Standards on Auditing*, paragraphs 15–16 and A20–A24

9. When this ISA expressly intends that a requirement or responsibility be fulfilled by the engagement partner, the term “the engagement partner shall ...” is used. In such circumstances, the engagement partner may need to obtain information from the firm or other members of the engagement team to fulfil the requirement. For example, the engagement partner may need to gather information from engagement team members about suspected breaches of relevant ethical requirements in accordance with paragraph 19. When the engagement partner is permitted to assign the design or performance of procedures, tasks or actions to appropriately skilled or suitably experienced members of the engagement team, the term “the engagement partner shall take responsibility for...” is used. Nevertheless, the engagement partner remains ultimately responsible, and therefore accountable, for compliance with the requirements of this ISA. (Ref: Para. A23–A25)

Effective Date

10. This ISA is effective for audits of financial statements for periods beginning on or after [Date].

Objective

11. The objective of the auditor is to manage quality at the engagement level to obtain reasonable assurance that quality has been achieved such that:
- (a) The auditor has fulfilled the auditor’s responsibilities, and has conducted the audit, in accordance with professional standards and applicable legal and regulatory requirements; and
 - (b) The auditor’s report issued is appropriate in the circumstances.

Definitions

12. For purposes of the ISAs, the following terms have the meanings attributed below:
- (a) Engagement partner⁷ – The partner, or other individual appointed by the firm, who is responsible for the audit engagement and its performance, and for the auditor’s report that is issued on behalf of the firm, and who, where required, has the appropriate authority from a professional, legal, or regulatory body.
 - (b) Engagement quality review – An objective evaluation of the significant judgments made by the engagement team and the conclusions reached thereon, performed by the engagement quality reviewer and completed on or before the date of the engagement report.
 - (c) Engagement quality reviewer – A partner, other individual in the firm, or an external individual appointed by the firm to perform the engagement quality review.
 - (d) Engagement team – All partners and staff performing the audit engagement, and any other individuals who perform audit procedures on the engagement, excluding an auditor’s external expert engaged by the firm or a network firm,⁸ and internal auditors who provide direct assistance on an engagement.⁹ (Ref: Para. A16–A25)

⁷ “Engagement partner,” “partner,” and “firm” should be read as referring to their public sector equivalents where relevant.

⁸ ISA 620, *Using the Work of an Auditor’s Expert*, paragraph 6(a), defines the term “auditor’s expert.”

⁹ 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.

- (e) Firm – A sole practitioner, partnership, or corporation or other entity of professional accountants, or public sector equivalent. (Ref: Para. A26)
- (f) Network firm – A firm or entity that belongs to a network. (Ref: Para. A27)
- (g) Network – A larger structure: (Ref: Para. A27)
 - (i) That is aimed at cooperation, and
 - (ii) That is clearly aimed at profit or cost-sharing or shares common ownership, control, or management, common quality management policies or procedures, common business strategy, the use of a common brand name, or a significant part of professional resources.
- (h) Partner – Any individual with authority to bind the firm with respect to the performance of a professional services engagement.
- (i) Personnel – Partners and staff.
- (j) Professional standards – International Standards on Auditing (ISAs) and relevant ethical requirements.
- (k) Relevant ethical requirements – Principles of professional ethics and ethical requirements that are applicable to professional accountants when undertaking the audit engagement. Relevant ethical requirements ordinarily comprise the provisions of the International Ethics Standards Board for Accountants' *International Code of Ethics for Professional Accountants (including International Independence Standards)* (IESBA Code) related to audits of financial statements, together with national requirements that are more restrictive.
- (l) Response (in relation to a system of quality management) – Policies or procedures designed and implemented by the firm to address a quality risk:
 - (i) Policies are statements of what should, or should not, be done to address a quality risk. Such statements may be documented, explicitly stated in communications or implied through actions and decisions.
 - (ii) Procedures are actions to implement policies.
- (m) Staff – Professionals, other than partners, including any experts the firm employs.

Requirements

Leadership Responsibilities for Managing and Achieving Quality on Audits

13. The engagement partner shall take overall responsibility for managing and achieving quality on the audit engagement, including taking responsibility for creating an environment for the engagement that emphasizes the firm's culture and expected behavior of engagement team members. In doing so, the engagement partner shall be sufficiently and appropriately involved throughout the audit engagement such that the engagement partner has the basis for determining whether the significant judgments made, and the conclusions reached, are appropriate given the nature and circumstances of the engagement. (Ref: Para. A28–A38)
14. In creating the environment described in paragraph 13, the engagement partner shall take responsibility for clear, consistent and effective actions being taken that reflect the firm's commitment

to quality and establish and communicate the expected behavior of engagement team members, including emphasizing: (Ref: Para. A31–A37)

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

15. If the engagement partner assigns the design or performance of procedures, tasks or actions related to a requirement of this ISA to other members of the engagement team to assist the engagement partner in complying with the requirements of this ISA, the engagement partner shall continue to take overall responsibility for managing and achieving quality on the audit engagement through direction and supervision of those members of the engagement team, and review of their work. (Ref: Para. 9, A38)

Relevant Ethical Requirements, Including Those Related to Independence

16. The engagement partner shall have an understanding of the relevant ethical requirements, including those related to independence, that are applicable given the nature and circumstances of the audit engagement. (Ref: Para. A39–A43, A49)
17. The engagement partner shall take responsibility for other members of the engagement team having been made aware of relevant ethical requirements that are applicable given the nature and circumstances of the audit engagement, and the firm’s related policies or procedures, including those that address: (Ref: Para. A23–A25, A41–A45)
- (a) Identifying, evaluating and addressing threats to compliance with relevant ethical requirements, including those related to independence;
 - (b) Circumstances that may cause a breach of relevant ethical requirements, including those related to independence, and the responsibilities of members of the engagement team when they become aware of breaches; and
 - (c) The responsibilities of members of the engagement team when they become aware of an instance of non-compliance with laws and regulations.¹⁰
18. If matters come to the engagement partner’s attention that indicate that a threat to compliance with relevant ethical requirements exists, the engagement partner shall evaluate the threats through complying with the firm’s policies or procedures, using relevant information from the firm, the engagement team or other sources, and take appropriate action. (Ref: Para. A44–A45)

¹⁰ ISA 250 (Revised), *Considerations of Laws and Regulations in an Audit of Financial Statements*

19. The engagement partner shall remain alert throughout the audit engagement, through observation and making inquiries as necessary, for breaches of relevant ethical requirements or the firm's related policies or procedures by members of the engagement team. (Ref: Para. A46)
20. If matters come to the engagement partner's attention through the firm's system of quality management, or from other sources, that indicate that relevant ethical requirements applicable to the nature and circumstances of the audit engagement have not been fulfilled, the engagement partner, in consultation with others in the firm, shall take appropriate action. (Ref: Para. A47)
21. Prior to dating the auditor's report, the engagement partner shall take responsibility for determining whether relevant ethical requirements, including those related to independence, have been fulfilled. (Ref: Para. A39 and A48)

Acceptance and Continuance of Client Relationships and Audit Engagements

22. The engagement partner shall determine that the firm's policies or procedures for the acceptance and continuance of client relationships and audit engagements have been followed, and that conclusions reached in this regard are appropriate. (Ref: Para. A50–A53, A59)
23. The engagement partner shall take into account information obtained in the acceptance and continuance process in planning and performing the audit engagement in accordance with the ISAs and complying with the requirements of this ISA. (Ref: Para. A54–A57)
24. If the engagement team obtains information that may have caused the firm to decline the audit engagement had that information been known by the firm prior to accepting or continuing the client relationship or specific engagement, the engagement partner shall communicate that information promptly to the firm, so that the firm and the engagement partner can take the necessary action. (Ref: Para. A58)

Engagement Resources

25. The engagement partner shall determine, given the nature and circumstances of the audit engagement and any changes that may arise during the engagement, that sufficient and appropriate resources to perform the engagement are assigned or made available to the engagement team by the firm in a timely manner. (Ref: Para. A60–A69, A71–A72, A76)
26. The engagement partner shall determine that members of the engagement team, and any auditor's external experts and internal auditors who provide direct assistance who are not part of the engagement team, collectively have the appropriate competence and capabilities, including sufficient time, to perform the audit engagement. (Ref: Para. A62, A70–A72)
27. If, as a result of complying with the requirements in paragraphs 25 and 26, the engagement partner determines that resources assigned or made available by the firm are insufficient or inappropriate in the circumstances of the audit engagement, the engagement partner shall take appropriate action, including communicating with appropriate personnel in the firm about the need to allocate or assign additional or alternative resources to the engagement. (Ref: Para. A73–A75)
28. The engagement partner shall take responsibility for using the resources assigned or made available to the engagement team appropriately, given the nature and circumstances of the audit engagement. (Ref: Para. A65)

Engagement Performance

Direction, Supervision and Review

29. The engagement partner shall take responsibility for the direction and supervision of the members of the engagement team and the review of their work.
30. The engagement partner shall determine that the nature, timing and extent of direction, supervision and review is: (Ref: Para A77–A85, A90–A93)
 - (a) Planned¹¹ and performed in accordance with the firm’s policies or procedures, professional standards and applicable legal and regulatory requirements;
 - (b) Responsive to the nature and circumstances of the audit engagement and the resources assigned or made available to the engagement team by the firm; and
 - (c) Planned and performed on the basis that the work performed by less experienced engagement team members is directed, supervised and reviewed by more experienced engagement team members.
31. The engagement partner shall review audit documentation at appropriate points in time during the audit engagement, including audit documentation relating to: (Ref: Para. A86–A89)
 - (a) Significant matters;¹²
 - (b) Significant judgments, including those relating to difficult or contentious matters identified during the audit engagement, and the conclusions reached; and
 - (c) Other matters that, in the engagement partner’s professional judgment, are relevant to the engagement partner’s responsibilities.
32. On or before the date of the auditor’s report, the engagement partner shall determine, through review of audit documentation and discussion with the engagement team, that sufficient appropriate audit evidence has been obtained to support the conclusions reached and for the auditor’s report to be issued. (Ref: Para. A86–A90)
33. Prior to dating the auditor’s report, the engagement partner shall review the financial statements and the auditor’s report, including, if applicable, the description of the key audit matters¹³ and related audit documentation to determine that the report to be issued will be appropriate in the circumstances.¹⁴
34. The engagement partner shall review, prior to their issuance, formal written communications to management, those charged with governance or regulatory authorities. (Ref: Para. A94)

Consultation

35. The engagement partner shall: (Ref: Para. A95–A98)
 - (a) Take responsibility for the engagement team undertaking consultation on:

¹¹ ISA 300, *Planning an Audit of Financial Statements*, paragraph 11

¹² ISA 230, *Audit Documentation*, paragraph 8

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

¹⁴ ISA 700 (Revised), *Forming an Opinion and Reporting on Financial Statements* or ISA 705 (Revised), *Modifications to the Opinion in the Independent Auditor’s Report*

- (i) Matters on which the firm’s policies or procedures require consultation, including difficult or contentious matters; and
 - (ii) Other matters that, in the engagement partner’s professional judgment, require consultation;
- (b) Determine that members of the engagement team have undertaken appropriate consultation during the audit engagement, both within the engagement team, and between the engagement team and others at the appropriate level within or outside the firm;
 - (c) Determine 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.

Engagement Quality Review

36. For audit engagements for which an engagement quality review is required, the engagement partner shall: (Ref: Para. A99)
- (a) Determine that an engagement quality reviewer has been appointed;
 - (b) Cooperate with the engagement quality reviewer and inform other members of the engagement team of their responsibility to do so;
 - (c) Discuss significant matters and significant judgments arising during the audit engagement, including those identified during the engagement quality review, with the engagement quality reviewer; and
 - (d) Not date the auditor’s report until the completion of the engagement quality review. (Ref: Para. A100–A103)

Differences of Opinion

37. If differences of opinion arise within the engagement team, or between the engagement team and the engagement quality reviewer or personnel performing activities within the firm’s system of quality management, including those who provide consultation, the engagement team shall follow the firm’s policies or procedures for dealing with and resolving such differences of opinion. (Ref: Para. A104–A105)
38. The engagement partner shall:
- (a) Take responsibility for differences of opinion being addressed and resolved in accordance with the firm’s policies or procedures;
 - (b) Determine that conclusions reached are documented and implemented; and
 - (c) Not date the auditor’s report until any differences of opinion are resolved.

Monitoring and Remediation

39. The engagement partner shall take responsibility for: (Ref: Para. A106–A109)
- (a) Obtaining an understanding of the results of the firm’s monitoring and remediation process, as communicated by the firm including, as applicable, the results of the monitoring and remediation process of the network or network firms;

- (b) Determining the relevance and effect on the audit engagement of the information referred to in paragraph 39(a) and take appropriate action; and
- (c) Remaining alert throughout the audit engagement for information that may be relevant to the firm's monitoring and remediation process and communicate such information to those responsible for the process.

Taking Overall Responsibility for Managing and Achieving Quality

40. Prior to dating the auditor's report, the engagement partner shall determine that the engagement partner has taken overall responsibility for managing and achieving quality on the audit engagement. In doing so, the engagement partner shall determine that: (Ref: Para. A110–A115)
- (a) The engagement partner's involvement has been sufficient and appropriate throughout the audit engagement such that the engagement partner has the basis for determining that the significant judgments made and the conclusions reached are appropriate given the nature and circumstances of the engagement; and
 - (b) The nature and circumstances of the audit engagement, any changes thereto, and the firm's related policies or procedures, have been taken into account in complying with the requirements of this ISA.

Documentation

41. The auditor shall include in the audit documentation:¹⁵ (Ref: Para. A113–A116)
- (a) Matters identified, relevant discussions with firm personnel, and conclusions reached with respect to:
 - (i) Fulfillment of responsibilities relating to relevant ethical requirements, including those related to independence.
 - (ii) The acceptance and continuance of the client relationship and audit engagement.
 - (b) The nature and scope of, and conclusions resulting from, consultations undertaken during the audit engagement and how such conclusions were implemented.
 - (c) If the audit engagement is subject to an engagement quality review, that the engagement quality review has been completed on or before the date of the auditor's report.

* * *

Application and Other Explanatory Material

Scope of this ISA (Ref: Para. 1)

- A1. This ISA applies to all audits of financial statements, including audits of group financial statements. ISA 600¹⁶ deals with special considerations that apply to group audits, in particular those that involve component auditors. ISA 600, adapted as necessary in the circumstances, may also be useful in an audit of financial statements when the engagement team includes individuals from a network firm or

¹⁵ ISA 230, paragraphs 8–11 and A6

¹⁶ ISA 600, *Special Considerations—Audits of Group Financial Statements (Including the Work of Component Auditors)*

from a firm that is not a network firm. For example, ISA 600 may be useful when involving such an individual to attend a physical inventory count or inspect property, plant and equipment at a remote location.

- A2. ISA 200 requires the auditor to comply with relevant ethical requirements, including those pertaining to independence, relating to financial statement audit engagements.¹⁷ Paragraphs 16–18 and A39–A49 of this ISA include requirements and guidance that address complying with relevant ethical requirements that are applicable given the nature and circumstances of the engagement, including those related to independence.

The Firm’s System of Quality Management and Role of Engagement Teams (Ref: Para. 2–5)

- A3. Proposed ISQM 1 deals with a firm’s responsibilities for its system of quality management.
- A4. Firms or national requirements may use different terminology or frameworks to describe components of a system of quality management. National requirements that deal with the firm’s responsibilities to design, implement and operate a system of quality management are at least as demanding as [proposed] ISQM 1 when they address the requirements of ISQM 1 and impose obligations on the firm to achieve the objective of [proposed] ISQM 1.

Implementing the Firm’s Responses to Quality Risks That Are Applicable to the Audit Engagement (Ref: Para. 4(a))

- A5. Quality management at the engagement level is supported by the firm’s system of quality management and informed by the specific nature and circumstances of the audit engagement. In accordance with [proposed] ISQM 1, the firm is responsible for communicating to relevant personnel, including the engagement team, about their responsibilities for implementing the firm’s responses that are applicable at the engagement level. For example, such firm-level responses may include policies or procedures to undertake consultations with designated personnel in certain situations involving complex technical or ethical matters, or to involve firm-designated experts in specific engagements to perform audit procedures related to particular matters (e.g., the firm may specify that firm-designated credit experts are to be involved in auditing expected credit loss allowances in all audits of financial institutions).
- A6. Firm-level responses may include policies or procedures established by a network, or by a firm or a group of firms within the same network (network requirements or network services are described further in [proposed] ISQM 1 within the “Network Requirements or Network Services” section). The requirements of this ISA are based on the premise that the firm is responsible for taking the necessary action to enable engagement teams to implement or use network resources or services or the work of network resources or services on the audit engagement.
- A7. Some firm-level responses to quality risks are not performed at the engagement level but are nevertheless relevant when complying with the requirements of this ISA. For example, when determining whether the members of the engagement team collectively have the appropriate competence and capabilities to perform the audit engagement, the engagement partner may be able to depend on the firm’s policies or procedures dealing with personnel recruitment and professional training. Other examples of firm-level responses that the engagement team may be able to depend on when complying with the requirements of this ISA include:

¹⁷ ISA 200, paragraph 14

- Information systems that support the firm’s monitoring of independence;
 - Information systems that support the acceptance and continuance of client relationships and audit engagements; and
 - Audit methodologies and related implementation tools and guidance.
- A8. Due to the specific nature and circumstances of each audit engagement and changes that may occur during the audit engagement, a firm cannot identify all quality risks that may arise at the engagement level or set forth all relevant and appropriate responses. Accordingly, the engagement team exercises professional judgment in determining whether to design and implement responses, beyond those set forth in the firm’s policies or procedures, at the engagement level to meet the objective of this ISA.¹⁸
- A9. The engagement team’s determination of whether engagement level responses are required (and if so, what those responses are) is influenced by the requirements of this ISA, the engagement team’s understanding of the nature and circumstances of the engagement and any changes during the audit engagement. For example, unanticipated circumstances may arise during the engagement that may cause the engagement partner to request the involvement of appropriately experienced personnel in addition to those initially assigned or made available by the firm in accordance with paragraph 27.
- A10. The relative balance of the engagement team’s efforts to comply with the requirements of this ISA (i.e., between implementing the firm’s responses and designing and implementing engagement specific responses beyond those set forth in the firm’s policies or procedures) may vary. For example, the firm may design an audit program to be used in circumstances that are applicable to the audit engagement (e.g., an industry specific audit program). Other than determining the timing and extent of procedures to be performed, there may be little or no need for supplemental audit procedures to be added to the audit program at the engagement level. Alternatively, the engagement team’s actions in complying with the engagement performance requirements of this ISA may be more focused on designing and implementing responses at the engagement level to deal with the specific nature and circumstances of the engagement (e.g., planning and performing procedures to address risks of material misstatement not contemplated by the firm’s audit programs).

Providing the Firm with Information from the Audit Engagement (Ref: Para 4(c))

- A11. Ordinarily, the engagement team may depend on the firm’s policies or procedures in complying with the requirements of this ISA, unless:
- The engagement team’s understanding or practical experience indicates that the firm’s policies or procedures will not effectively address the nature and circumstances of the engagement; or
 - Information provided by the firm or other parties, about the effectiveness of such policies or procedures suggests otherwise (e.g., information provided by the firm’s monitoring and remediation processes or an external inspection process indicates that the firm’s policies or procedures are not operating effectively).
- A12. If the engagement partner becomes aware (including through being informed by other members of the engagement team) that the firm’s responses to quality risks are deficient in the context of the specific engagement or the engagement partner is unable to depend on the firm’s policies or procedures,

¹⁸ ISA 200 requires the auditor to exercise professional judgment in planning and performing an audit of financial statements.

the engagement partner communicates such information promptly to the firm in accordance with paragraph 39(c) as such information is relevant to the firm’s monitoring and remediation process. For example, if an engagement team member identifies that an audit software program has a security weakness, timely communication of such information to the appropriate individuals within the firm enables the firm to take steps to update and reissue the audit program. See also paragraph A65 in respect of sufficient and appropriate resources.

Information Relevant to Quality Management at the Engagement Level (Ref: Para. 5)

A13. Complying with the requirements in other ISAs may provide information that is relevant to quality management at the engagement level. For example, the understanding of the entity and its environment required to be obtained under ISA 315 (Revised 2019)¹⁹ provides information that may be relevant to complying with the requirements of this ISA. Such information may be relevant to the determination of:

- The nature of resources to deploy for specific audit areas, such as the use of appropriately experienced team members for high risk areas, or the involvement of experts to deal with complex matters;
- The amount of resources to allocate to specific audit areas, such as the number of team members assigned to attend the physical inventory count at multiple locations;
- The nature, timing and extent of review of the work performed by members of the team based on the number and significance of the assessed risks of material misstatement; or
- The allocation of the budgeted audit hours, including allocating more time, and the time of more experienced engagement team members to those areas where there are more risks of material misstatement or the identified risks are assessed as higher.

Considerations Specific to Smaller Firms (Ref: Para. 2–4, 8)

A14. In a smaller firm, the design and implementation of many responses to the firm’s quality risks, may be most effectively addressed by the engagement partner at the engagement level (i.e., given the nature and circumstances of the firm and the engagements it performs, there may be less need for firm-level responses to many of the firm’s quality risks). Additionally, a smaller firm’s policies or procedures may be less formal. For example, in a very small firm with a relatively small number of audit engagements, the firm may determine that there is no need to establish a firm wide system to monitor independence, and rather, independence will be monitored at the individual engagement level by the engagement partner.

A15. The requirements relating to direction, supervision and review of the work of other members of the engagement team are only relevant if there are members of the engagement team other than the engagement partner.

Definitions

Engagement Team (Ref: Para. 12(d))

A16. Engagement teams may be organized in a variety of ways. For example, engagement team members may be located together or across different geographic locations, and may be organized in groups

¹⁹ ISA 315 (Revised 2019), *Identifying and Assessing the Risks of Material Misstatement*

by the activity they are performing. Regardless of how the engagement team is organized, any individual who performs audit procedures²⁰ on the audit engagement is a member of the engagement team.

- A17. The definition of an engagement team focuses on individuals who perform audit procedures on the audit engagement. Audit evidence, which is necessary to support the auditor’s opinion and report, is primarily obtained from audit procedures performed during the course of the audit.²¹ Audit procedures comprise risk assessment procedures²² and further audit procedures.²³ As explained in ISA 500, audit procedures include inspection, observation, confirmation, recalculation, reperformance, analytical procedures and inquiry, often performed in some combination.²⁴ Other ISAs may also include specific procedures to obtain audit evidence, for example, ISA 520.²⁵
- A18. Engagement teams include individuals from the firm who perform audit procedures and may include individuals who perform audit procedures from:
- (a) A network firm.
 - (b) A firm that is not a network firm.
 - (c) A service provider.

For example, an individual from a network firm or from a firm that is not a network firm, may perform audit procedures on the financial information of a component in a group audit engagement, attend a physical inventory count or inspect physical fixed assets at a remote location.

- A19. Engagement teams may also include individuals from service delivery centers who perform audit procedures. For example, the firm may determine that specific tasks that are repetitive or specialized in nature can be performed by a group of appropriately skilled personnel and the engagement team may therefore include such individuals. Service delivery centers may be established at the firm level, at the network level, or by a firm or a group of firms from within the same network. For example, a centralized function may be used to facilitate external confirmation procedures.
- A20. Engagement teams may include individuals with expertise in a specialized area of accounting or auditing who perform audit procedures on the audit engagement, for example, individuals with expertise in accounting for income taxes, or in analyzing complex information produced by automated tools and techniques for the purpose of identifying unusual or unexpected relationships. An individual with such expertise is not a member of the engagement team if that individual’s involvement with the engagement is limited to consultation. Consultations are addressed in paragraphs 35 and A95–A98.

²⁰ ISA 500, *Audit Evidence*, paragraph A10

²¹ ISA 200, paragraph A30

²² ISA 315 (Revised 2019) provides requirements related to risk assessment procedures

²³ ISA 330, *The Auditor’s Responses to Assessed Risks*, provides requirements related to further audit procedures, including tests of controls and substantive procedures

²⁴ ISA 500, *Audit Evidence*, paragraphs A14–A25

²⁵ ISA 520, *Analytical Procedures*

- A21. If the audit engagement is subject to an engagement quality review, the engagement quality reviewer, and any other individuals performing the engagement quality review, are not members of the engagement team. Such individuals may be subject to specific independence requirements.
- A22. An auditor's external expert whose work is used in the engagement and an internal auditor providing direct assistance are not members of the engagement team.²⁶ ISA 610 (Revised) 2013) and ISA 620 provide requirements and guidance for the auditor when using the work of internal auditors in a direct assistance capacity or when using the work of an external expert. Compliance with these ISAs requires the auditor to perform audit procedures on the work of an auditor's expert and obtain sufficient appropriate audit evidence on the work performed by an internal auditor providing direct assistance.

The Application of Firm Policies or Procedures by Members of the Engagement Team (Ref: Para. 9, 17)

- A23. As described in paragraph 4, within the context of the firm's system of quality management, the engagement team is responsible for implementing the firm's policies or procedures that are applicable to the audit engagement. If the engagement team includes individuals who are from a network firm or a firm that is not a network firm, the firm's policies or procedures may be different, or different actions may need to be taken by members of the engagement team to implement the firm's policies or procedures relevant to the engagement.
- A24. In particular, firm policies or procedures may require the firm or the engagement partner to take different actions from those applicable to personnel within the firm when obtaining an understanding of whether an individual from a network firm or a firm that is not a network firm:
- Has the appropriate competence and capabilities, including sufficient time, to perform the audit engagement. For example, the individual would not be subject to the firm's recruitment and training processes and therefore the firm's policies or procedures may state that this determination can be made through other actions such as obtaining information from the individual's professional body. Paragraphs 19 and A38 of ISA 600 contain guidance on obtaining an understanding of the competence and capabilities of component auditors.
 - Understands the ethical requirements that are relevant to the group audit engagement. For example, the individual would not be subject to the firm's training in respect of the firm's policies or procedures for relevant ethical requirements. The firm's policies or procedures may state that this understanding is obtained through other actions such as providing information, manuals, or guides containing the provisions of the relevant ethical requirements applicable to the audit engagement to the component auditor.
 - Will confirm independence. For example, individuals from a network firm may not be able to complete independence declarations directly on the firm's independence systems. The firm's policies or procedures may state that such individuals can provide evidence of their independence in relation to the audit engagement in other ways, such as written confirmation.
- A25. When firm policies or procedures require specific activities to be undertaken in certain circumstances (e.g., in relation to an audit engagement where the firm's policies or procedures require consultation on a matter), it may be necessary for the firm's policies or procedures to be communicated to individuals who are not firm personnel so that such individuals are able to alert the engagement

²⁶ See ISA 620, paragraphs 12–13 and ISA 610 (Revised 2013), paragraphs 21–25.

partner about the circumstance if it arises, and the engagement partner is able to follow the firm's policies or procedures. For example, in a group audit engagement, if a component auditor is performing audit procedures on the financial information of a component and identifies a difficult or contentious matter that is relevant to the group financial statements and subject to consultation²⁷ under the group auditor's policies or procedures, the component auditor is able to alert the group engagement team about the matter.

Firm (Ref: Para. 12(e))

A26. The definition of "firm" in relevant ethical requirements may differ from the definition set out in this ISA. For example, the IESBA Code defines the "firm" as:

- (a) A sole practitioner, partnership or corporation of professional accountants;
- (b) An entity that controls such parties through ownership, management or other means; and
- (c) An entity controlled by such parties through ownership, management or other means.

In complying with the requirements in this ISA, the definitions used in the relevant ethical requirements apply insofar as is necessary to interpret those ethical requirements.

"Network" and "Network Firm" (Ref: Para. 12(f)–12(g))

A27. The definitions of "network" or "network firm" in relevant ethical requirements may differ from those set out in this ISA. The IESBA Code also provides guidance in relation to the terms "network" and "network firm." Networks and the firms within the network may be structured in a variety of ways, and are in all cases external to the firm. The provisions in this ISA in relation to networks apply to any structures or organizations that do not form part of the firm, but that exist within the network.

Leadership Responsibilities for Managing and Achieving Quality on Audits (Ref: Para. 13–15)

Taking Overall Responsibility for Managing and Achieving Quality

A28. Proposed ISQM 1 requires the firm to establish quality objectives that address the aspects of the firm's environment including the firm's culture, decision-making process, actions, organizational structure and leadership. The engagement partner's responsibility for managing and achieving quality is supported by a firm culture that promotes the conduct of quality audit engagements. In addressing the requirements in paragraphs 13 and 14 of this ISA, the engagement partner may communicate directly and reinforce this communication through personal conduct and actions (e.g., leading by example). A commitment to quality is further shaped and reinforced by the engagement team members as they demonstrate expected behaviors when performing the engagement.

A29. The nature and extent of the actions of the engagement partner to reflect the firm's commitment to quality may depend on a variety of factors including the size, structure, geographical dispersion and complexity of the firm and the engagement team, and the nature and circumstances of the audit engagement. With a smaller engagement team with few engagement team members, influencing the desired culture through direct interaction and conduct may be sufficient, whereas for a larger engagement team that is dispersed over many locations, more formal communications may be necessary.

²⁷ See paragraph 32.

Sufficient and Appropriate Involvement

A30. Being sufficiently and appropriately involved throughout the audit engagement may be demonstrated by the engagement partner in different ways, including:

- Taking responsibility for the nature, timing and extent of the direction and supervision of members of the engagement team, and the review of their work in complying with the requirements of this ISA; and
- Varying the nature, timing and extent of such direction, supervision and review in the context of the nature and circumstances of the engagement.

Communication

A31. Communication is the means through which the engagement team share relevant information on a timely basis to comply with the requirements of this ISA, thereby contributing to the achievement of quality on the audit engagement. Communication may be between or among members of the engagement team, or with:

- (a) The firm, (e.g., personnel performing activities within the firm's system of quality management, including those assigned ultimate or operational responsibility for the firm's system of quality management);
- (b) Others involved in the audit (e.g., an auditor's external expert²⁸ or internal auditors who provide direct assistance²⁹); and
- (c) Parties that are external to the firm (e.g., management, those charged with governance or regulatory authorities).

A32. The firm may use technology to facilitate more effective communication between different parties. For example, to support appropriate direction, supervision and review, the firm may use technological resources in the form of information technology (IT) applications to facilitate the communication between the members of the engagement team when they are performing work across different geographical locations.

A33. The nature and circumstances of the audit engagement may affect the engagement partner's decisions regarding the most appropriate means of effective communication with the members of the engagement team. For example, in-person and more frequent interactions are likely to be a more effective way to direct and supervise less experienced members of the engagement team.

Professional Skepticism

A34. The engagement partner is responsible for emphasizing the importance of each engagement team member exercising professional skepticism throughout the audit engagement. Conditions inherent in some audit engagements can create pressures on the engagement team that may impede the appropriate exercise of professional skepticism when designing and performing audit procedures and evaluating audit evidence. Accordingly, when developing the overall audit strategy in accordance with ISA 300, the engagement team may need to consider whether such conditions exist in the audit

²⁸ See ISA 620, paragraphs 11(c) and A30.

²⁹ See ISA 610 (Revised 2013), paragraph A41.

engagement and, if so, what actions the firm or the engagement team may need to undertake to mitigate such impediments.

A35. Impediments to the exercise of professional skepticism at the engagement level may include, but are not limited to:

- Budget constraints, which may discourage the use of sufficiently experienced or technically qualified resources, including experts, necessary for audits of entities where technical expertise or specialized skills are needed for effective understanding, assessment of and responses to risks and informed questioning of management.
- Tight deadlines, which may negatively affect the behavior of those who perform the work as well as those who direct, supervise and review. For example, external time pressures may create restrictions to analyzing complex information effectively.
- Lack of cooperation or undue pressures imposed by management, which may negatively affect the engagement team's ability to resolve complex or contentious issues.
- Insufficient understanding of the entity and its environment, its system of internal control and the applicable financial reporting framework, which may constrain the ability of the engagement team to make appropriate judgments and an informed questioning of management's assertions.
- Difficulties in obtaining access to records, facilities, certain employees, customers, vendors or others, which may cause the engagement team to bias the selection of sources of audit evidence and seek audit evidence from sources that are more easily accessible.
- Overreliance on templates and automated tools.

A36. Unconscious or conscious auditor biases may affect the engagement team's professional judgments, including for example, in the design and performance of audit procedures, or the evaluation of audit evidence. Examples of unconscious auditor biases that may impede the exercise of professional skepticism, and therefore the reasonableness of the professional judgments made by the engagement team in complying with the requirements of this ISA, may include:

- Availability bias, which is a tendency to place more weight on events or experiences that immediately come to mind or are readily available than on those that are not.
- Confirmation bias, which is a tendency to place more weight on information that corroborates an existing belief than information that contradicts or casts doubt on that belief.
- Overconfidence bias, which is a tendency to overestimate one's own ability to make accurate assessments of risk or other judgments or decisions.
- Anchoring bias, which is a tendency to use an initial piece of information as an anchor against which subsequent information is inadequately assessed.
- Automation bias, which is a tendency to favor output generated from automated systems, even when human reasoning or contradictory information raises questions as to whether such output is reliable or fit for purpose.

A37. Possible actions that the engagement team may take to mitigate impediments to the exercise of professional skepticism at the engagement level may include:

- Remaining alert to changes in the nature or circumstances of the audit engagement that necessitate additional or different resources for the engagement, and requesting additional or different resources from those individuals within the firm responsible for allocating or assigning resources to the engagement.
- Explicitly alerting the engagement team to instances or situations when vulnerability to unconscious or conscious auditor biases may be greater (e.g., areas involving greater judgment) and emphasizing the importance of seeking advice from more experienced members of the engagement team in planning and performing audit procedures.
- Changing the composition of the engagement team, for example, requesting that more experienced individuals are assigned to the engagement to obtain greater skills or knowledge or specific expertise.
- Involving more experienced members of the engagement team when dealing with members of management who are difficult or challenging to interact with.
- Involving members of the engagement team with specialized skills and knowledge or an auditor's expert to assist the engagement team with complex or subjective areas of the audit.
- Modifying the nature, timing and extent of direction, supervision or review by involving more experienced engagement team members, more in-person oversight on a more frequent basis and more in-depth reviews of certain working papers for:
 - Complex or subjective areas of the audit;
 - Areas that pose risks to achieving quality on the audit engagement; and
 - Areas with a fraud risk or a risk of non-compliance with laws or regulations.
- Setting expectations for:
 - Less experienced members of the engagement team to seek advice frequently and in a timely manner from more experienced engagement team members or the engagement partner; and
 - More experienced members of the engagement team to be available to less experienced members of the engagement team throughout the audit engagement and to respond positively and in a timely manner to their insights, requests for advice or assistance.
- Communicating with those charged with governance when management imposes undue pressure or the engagement team experiences difficulties in obtaining access to records, facilities, certain employees, customers, vendors or others from whom audit evidence may be sought.

Assigning Procedures, Tasks, or Actions to Other Members of the Engagement Team (Ref: Para. 15)

A38. Being sufficiently and appropriately involved throughout the audit engagement when procedures, tasks or actions have been assigned to other members of the engagement team may be demonstrated by the engagement partner in different ways, including:

- Informing assignees about the nature of their responsibilities and authority, the scope of the work being assigned and the objectives thereof; and to provide any other necessary instructions and relevant information;
- Direction and supervision of the assignees; and
- Review of the assignees' work to evaluate the conclusions reached, in addition to the requirements in paragraphs 29–34.

Relevant Ethical Requirements, Including Those Related to Independence (Ref: Para. 16–21)

Relevant Ethical Requirements

- A39. ISA 200³⁰ requires that the auditor comply with relevant ethical requirements, including those pertaining to independence, relating to financial statement audit engagements. Relevant ethical requirements may vary depending on the nature and circumstances of the engagement. For example, certain requirements related to independence may be applicable only when performing audits of listed entities. ISA 600 includes additional requirements and guidance to those in this ISA regarding communications about relevant ethical requirements with component auditors.
- A40. Based on the nature and circumstances of the audit engagement, certain relevant ethical requirements or aspects of law or regulation, may be significant to the engagement, for example law or regulation dealing with money laundering, corruption, or bribery.
- A41. The information and communication component of the firm's system of quality management and the resources provided by the firm may assist the engagement team in understanding and fulfilling relevant ethical requirements applicable to the nature and circumstances of the audit engagement in accordance with paragraphs 16–21. For example:
- Communicating the independence requirements to all engagement team members subject to independence requirements, as applicable.
 - Providing training for engagement team members on relevant ethical requirements.
 - Establishing manuals and guides (i.e., intellectual resources) containing the provisions of the relevant ethical requirements and guidance on how they are applied in the circumstances of the firm and the engagements it performs.
 - Assigning personnel (i.e., human resources) to manage and monitor compliance with relevant ethical requirements (e.g., ISQM 1 requires that the firm obtain, at least annually, a documented confirmation of compliance with the independence requirements from all personnel required by relevant ethical requirements to be independent) or to provide consultation on matters related to relevant ethical requirements.
 - Establishing policies or procedures for engagement team members to communicate relevant information to appropriate parties within the firm or to the engagement partner, such as requirements for engagement team members to:

³⁰ ISA 200, paragraphs 14 and A16–A19

- Communicate information about client engagements and the scope of services, including non-assurance services, to enable the firm to identify threats to independence during the period of the engagement and during the period covered by the subject matter.
- Communicate circumstances and relationships that may create a threat to independence, so that the firm can evaluate whether such a threat is at an acceptable level and if it is not, address the threat by eliminating it or reducing it to an acceptable level.
- Promptly communicate any breaches of the relevant ethical requirements, including those related to independence.

A42. The engagement partner may take into account the information, communication, and resources described in paragraph A41 when determining whether the engagement partner may depend on a firm policies or procedures in complying with relevant ethical requirements.

A43. Open and robust communication between the members of the engagement team about relevant ethical requirements may also assist in:

- Drawing the attention of engagement team members to relevant ethical requirements that may be of particular significance to the audit engagement; and
- Keeping the engagement partner informed about matters relevant to the engagement team's understanding and fulfillment of relevant ethical requirements and the firm's related policies or procedures.

Identifying and Evaluating Threats to Compliance with Relevant Ethical Requirements (Ref: Para. 17–18)

A44. In accordance with [proposed] ISQM 1, the firm's responses to address the quality risks in relation to relevant ethical requirements, including those related to independence for engagement team members, include policies or procedures that address the identification and evaluation of threats to compliance with the relevant ethical requirements and how identified threats should be addressed.

A45. Relevant ethical requirements may contain provisions regarding the identification and evaluation of threats and how they should be dealt with. For example, the IESBA Code explains that a self-interest threat to compliance with the fundamental principle of professional competence and due care may arise if the fee quoted for an audit engagement is so low that it might be difficult to perform the engagement in accordance with professional standards.³¹

Breaches of Relevant Ethical Requirements (Ref: Para. 19)

A46. In accordance with [proposed] ISQM 1, the firm is required to establish policies or procedures that address the identification, communication, evaluation and reporting of breaches and actions to address the causes and consequences of the breaches.

³¹ IESBA Code, paragraph 330.3, A2

Taking Appropriate Action (Ref: Para. 20)

A47. Appropriate actions may include, for example:

- Following the firm's policies or procedures regarding breaches of relevant ethical requirements, including communicating to or consulting with the appropriate personnel within the firm so that appropriate action can be taken, including as applicable, disciplinary action(s).
- Communicating with those charged with governance.
- Communicating with regulatory authorities. In some circumstances, communication with regulatory authorities may be required by law or regulation.
- Seeking legal advice.
- Withdrawing from the audit engagement, when withdrawal is possible under applicable law or regulation.

Prior to Dating the Auditor's Report (Ref: Para. 21)

A48. ISA 700 (Revised) requires that the auditor's report include a statement that the auditor is independent of the entity in accordance with the relevant ethical requirements relating to the audit, and that the auditor has fulfilled the auditor's other ethical responsibilities in accordance with these requirements.³² Performing the procedures required by paragraphs 16–21 of this ISA provides the basis for these statements in the auditor's report.

Considerations Specific to Public Sector Entities

A49. Statutory measures may provide safeguards for the independence of public sector auditors. However, public sector auditors or audit firms carrying out public sector audits on behalf of the statutory auditor may, depending on the terms of the mandate in a particular jurisdiction, need to adapt their approach to promote compliance with the underlying principles of paragraph 16. This may include, where the public sector auditor's mandate does not permit withdrawal from the audit engagement, disclosure through a public report of circumstances that have arisen that would, if they were in the private sector, lead the auditor to withdraw.

Acceptance and Continuance of Client Relationships and Audit Engagements (Ref: Para. 22–24)

A50. Proposed ISQM 1 requires the firm to establish quality objectives that address the acceptance and continuance of client relationships and specific engagements that are appropriate in the circumstances.

A51. Information such as the following may assist the engagement partner in determining whether the conclusions reached regarding the acceptance and continuance of client relationships and audit engagements are appropriate:

- The integrity and ethical values of the principal owners, key management and those charged with governance of the entity;
- Whether sufficient and appropriate resources are available to perform the engagement;

³² ISA 700 (Revised), *Forming an Opinion and Reporting on Financial Statements*, paragraph 28(c)

- Whether management and those charged with governance have acknowledged their responsibilities in relation to the engagement;
- Whether the engagement team has the competence and capabilities, including sufficient time, to perform the engagement; and
- Whether significant matters that have arisen during the current or previous engagement have implications for continuing the engagement.

A52. Under [proposed] ISQM 1, for acceptance and continuance decisions, the firm is required to make appropriate judgments about whether it will have access to information to perform the engagement or to the persons who provide such information. The engagement partner may use the information considered by the firm in this regard in determining whether the conclusions reached regarding the acceptance and continuance of client relationships and audit engagements are appropriate. If the engagement partner has concerns regarding the appropriateness of the conclusions reached, the engagement partner may discuss the basis for those conclusions with those involved in the acceptance and continuance process.

A53. If the engagement partner is directly involved throughout the firm's acceptance and continuance process, the engagement partner will be aware of the information obtained or used by the firm, in reaching the related conclusions. Such direct involvement may also provide a basis for the engagement partner's determination that the firm's policies or procedures have been followed and that the conclusions reached are appropriate.

A54. Information obtained during the acceptance and continuance process may assist the engagement partner in complying with the requirements of this ISA and making informed decisions about appropriate courses of action. Such information may include:

- Information about the size, complexity and nature of the entity, including whether it is a group audit, the industry in which it operates and the applicable financial reporting framework;
- The entity's timetable for reporting, such as at interim and final stages;
- In relation to group audits, the nature of the control relationships between the parent and its components; and
- Whether there have been changes in the entity or in the industry in which the entity operates since the previous audit engagement that may affect the nature of resources required, as well as the manner in which the work of the engagement team will be directed, supervised and reviewed.

A55. Information obtained during acceptance and continuance may also be relevant in complying with the requirements of other ISAs, as well as this ISA, for example with respect to:

- Establishing an understanding of the terms of the audit engagement, as required by ISA 210;³³
- Identifying and assessing risks of material misstatement, whether due to error or fraud, in accordance with ISA 315 (Revised 2019) and ISA 240;³³

³³ ISA 240, *The Auditor's Responsibilities Relating to Fraud in an Audit of Financial Statements*

- Understanding the group, its components and their environments, in the case of an audit of group financial statements in accordance with ISA 600, and directing, supervising and reviewing the work of component auditors;
 - Determining whether, and how, to involve an auditor’s expert in accordance with ISA 620; and
 - The entity’s governance structure in accordance with ISA 260³⁴ and ISA 265.³⁵
- A56. Law, regulation, or relevant ethical requirements may require the successor auditor to request, prior to accepting the audit engagement, the predecessor auditor to provide known information regarding any facts or circumstances that, in the predecessor auditor’s judgment, the successor auditor needs to be aware of before deciding whether to accept the engagement. In some circumstances, the predecessor auditor may be required, on request by the proposed successor auditor, to provide information regarding identified or suspected non-compliance with laws and regulations to the proposed successor auditor. For example, if the predecessor auditor has withdrawn from the engagement as a result of identified or suspected non-compliance with laws and regulations, the IESBA Code requires that the predecessor auditor, on request by a proposed successor auditor, provide all such facts and other information concerning such non-compliance that, in the predecessor auditor’s opinion, the proposed successor auditor needs to be aware of before deciding whether to accept the audit appointment.
- A57. In circumstances when the firm is obligated by law or regulation to accept or continue an audit engagement, the engagement partner may take into account information obtained by the firm about the nature and circumstances of the engagement in complying with the requirement in paragraph 23.
- A58. In deciding on the necessary action in accordance with paragraph 24, the engagement partner and the firm may conclude that it is appropriate to continue with the audit engagement, and if so, what additional steps are necessary at the engagement level (e.g., the assignment of more staff or staff with specific expertise). If the engagement partner has further concerns or is not satisfied that the matter has been appropriately dealt with, the firm’s policies or procedures for resolving differences of opinion may be applicable.

Considerations Specific to Public Sector Entities (Ref: Para. 22–24)

- A59. In the public sector, auditors may be appointed in accordance with statutory procedures and the public sector auditor may not need to establish all policies or procedures regarding the acceptance and continuance of audit engagements. Nevertheless, the requirements and considerations for the acceptance and continuance of client relationships and engagements as set out in paragraphs 22–24 and A50–A55 may be valuable to public sector auditors in performing risk assessments and in carrying out reporting responsibilities.

Engagement Resources (Ref: Para. 25–28)

A60. Under [proposed] ISQM 1, the resources assigned, allocated or made available by the firm to support the performance of audit engagements include:

- Human resources;

³⁴ ISA 260 (Revised), *Communication with Those Charged with Governance*

³⁵ ISA 265, *Communicating Deficiencies in Internal Control to Those Charged with Governance and Management*

- Technological resources; and
- Intellectual resources.

A61. A relevant consideration for the engagement partner, in complying with the requirements in paragraphs 25 and 26, may be whether the resources assigned or made available to the engagement team enable fulfillment of relevant ethical requirements, including ethical principles such as professional competence and due care.

Human Resources

A62. Human resources assigned or made available by the firm include members of the engagement team (see also paragraphs A16–A22) and, where applicable, an auditor’s external expert and individuals from within the entity’s internal audit function who provide direct assistance on the audit.

Technological Resources

A63. The use of technological resources on the audit engagement may assist the auditor in obtaining sufficient appropriate audit evidence. Technology may allow the auditor to more effectively and efficiently manage the audit. Technology may also allow the auditor to evaluate large amounts of data more easily to, for example, provide deeper insights, identify unusual trends or more effectively challenge management’s assertions, which enhances the ability of the auditor to exercise professional skepticism. Technology may also be used to conduct meetings and provide communication tools to the engagement team. Inappropriate use of such technological resources may, however, increase the risk of overreliance on the information produced for decision making purposes, or may create threats to complying with relevant ethical requirements, for example, requirements related to confidentiality.

A64. The firm’s policies or procedures may set forth required considerations or responsibilities for the engagement team when using firm approved technology to perform audit procedures and may require the involvement of individuals with specialized skills or expertise in evaluating or analyzing the output.

A65. The firm’s policies or procedures may specifically prohibit the use of certain technological resources (e.g., software that has not yet been specifically approved for use by the firm). Alternatively, the firm’s policies or procedures may require the engagement team to take certain actions before using a technological resource that is not firm approved to determine it is appropriate for use, for example by requiring:

- The engagement team to have appropriate competence and capabilities to use the technological resource.
- Specific documentation to be included in the audit file.
- Testing the operation and security of the technological resource.

A66. The engagement partner may exercise professional judgment in considering whether the use of the resource on the audit engagement is appropriate in the context of the engagement, and if so, how the technological resource is to be used. Factors that may be considered in determining whether a particular technological resource, that has not been specifically approved for use by the firm, is appropriate for use in the audit engagement include whether:

- Use and security of the technological resource complies with the firm’s policies or procedures.
- The technological resource operates as intended.
- Personnel have the competence and capabilities required to use the technological resource.

Intellectual Resources

- A67. Intellectual resources include, for example, audit methodologies, implementation tools, auditing guides, model programs, templates, checklists or forms.
- A68. The use of intellectual resources on the audit engagement may facilitate the consistent application and understanding of professional standards, law and regulation, and related firm policies or procedures. For this purpose, the engagement team may be required, in accordance with the firm’s policies or procedures, to use the firm’s audit methodology and specific tools and guidance. The engagement team may also consider whether the use of other intellectual resources is appropriate and relevant based on the nature and circumstances of the engagement, for example, an industry-specific methodology or related guides and performance aids.

Sufficient and Appropriate Resources to Perform the Engagement (Ref: Para. 25)

- A69. In determining whether sufficient and appropriate resources to perform the engagement have been assigned or made available to the engagement team by the firm, ordinarily the engagement partner may depend on the firm’s related policies or procedures (including resources) as described in paragraph A7. For example, based on information communicated by the firm, the engagement partner may be able to depend on the firm’s technological development and maintenance programs when using firm-approved technology to perform audit procedures.

Competence and Capabilities of the Engagement Team (Ref: Para. 26)

- A70. When determining that the engagement team has the appropriate competence and capabilities, the engagement partner may take into consideration such matters as the team’s:
- Understanding of, and practical experience with, audit engagements of a similar nature and complexity through appropriate training and participation.
 - Understanding of professional standards and applicable legal and regulatory requirements.
 - Expertise in specialized areas of accounting or auditing.
 - Expertise in information technology used by the entity or automated tools or techniques that are to be used by the engagement team in planning and performing the audit engagement.
 - Knowledge of relevant industries in which the entity being audited operates.
 - Ability to exercise professional skepticism and professional judgment.
 - Understanding of the firm’s policies or procedures.

Project Management

- A71. In situations where there are many engagement team members, for example on larger, or more complex, audit engagements, the engagement partner may involve an individual from firm personnel who has specialized skills or knowledge in project management, supported by appropriate

technological and intellectual resources of the firm. Conversely, in an audit of a less complex entity with few engagement team members, project management may be achieved by a member of the engagement team through less formal means.

A72. Project management techniques and tools may support the engagement team in managing the quality of the audit engagement by, for example:

- Increasing the engagement team's ability to exercise professional skepticism through alleviating budget or time constraints that may otherwise impede the exercise of professional skepticism;
- Facilitating timely performance of audit work to effectively manage time constraints at the end of the audit process when more difficult or contentious matters may arise;
- Monitoring the progress of the audit against the audit plan,³⁶ including the achievement of key milestones, which may assist the engagement team in being proactive in identifying the need for making timely adjustments to the audit plan and the assigned resources; or
- Facilitating communication among members of the engagement team, for example, coordinating arrangements with component auditors and auditor's experts.

Insufficient or Inappropriate Resources (Ref: Para. 27)

A73. Proposed ISQM 1 requires that the firm's quality objectives include that the firm's strategic decisions and actions, including financial and operational priorities, reflect the firm's commitment to quality and do not undermine the firm's role in serving the public interest by consistently performing quality engagements. However, in certain circumstances, the firm's financial and operational priorities may place constraints on the resources assigned or made available to the engagement team (see also paragraph A45). In such circumstances, these constraints do not override the engagement partner's responsibility for achieving quality at the engagement level, including for determining that the resources assigned or made available by the firm are sufficient and appropriate to perform the audit engagement.

A74. The engagement partner's determination of whether additional engagement level resources are required is a matter of professional judgment and is influenced by the requirements of this ISA and the nature and circumstances of the audit engagement. As described in paragraph A12, in certain circumstances, the engagement partner may determine that the firm's responses to quality risks are deficient in the context of the specific engagement, including that certain resources assigned to the engagement team are insufficient. In those circumstances, the engagement partner takes appropriate action, including communicating such information to the appropriate individuals within the firm in accordance with paragraph 27 and paragraph 39(a). For example, if an audit software program provided by the firm has not incorporated new or revised audit procedures in respect of recently issued industry regulation, timely communication of such information to the appropriate individuals within the firm enables the firm to take steps to update and reissue the software promptly or to provide an alternative resource that enables the engagement team to comply with the new regulation in the performance of the audit engagement.

³⁶ See ISA 300, *Planning an Audit of Financial Statements*, paragraph 9.

A75. If the engagement partner determines that the resources assigned or made available are insufficient or inappropriate given the nature and circumstances of the engagement and additional or alternative resources have not been made available by the firm, the engagement partner is required to take appropriate action. In such cases, appropriate actions may include:

- Changing the planned approach to the nature, timing and extent of direction, supervision and review (see also paragraph A92).
- Discussing an extension to reporting deadlines with management or those charged with governance, when an extension is possible under applicable law or regulation.
- Following the firm's policies or procedures for resolving differences of opinion if the engagement partner does not obtain the necessary resources for the audit engagement.
- Following the firm's policies or procedures for withdrawing from the audit engagement, when withdrawal is possible under applicable law or regulation.

Considerations Specific to Public Sector Entities (Ref: Para. 25–28)

A76. In the public sector, specialized skills may be necessary to discharge the terms of the audit mandate in a particular jurisdiction. Such skills may include an understanding of the applicable reporting arrangements, including reporting to the legislature or other governing body or reporting in the public interest. The wider scope of a public sector audit may include, for example, some aspects of performance auditing.

Engagement Performance

Direction, Supervision and Review (Ref: Para. 30)

A77. Under [proposed] ISQM 1, the firm is required to establish policies or procedures addressing the nature, timing and extent of the direction and supervision of engagement teams and review of their work, including that such direction, supervision and review is planned and performed on the basis that the work performed by less experienced members of the engagement team is directed, supervised and reviewed in a timely manner by more experienced engagement team members.

A78. Direction and supervision of the engagement team and the review of the work of the engagement team are firm-level responses that are implemented at the engagement level, of which the nature, timing and extent may be further tailored by the engagement partner in managing the quality of the audit engagement. Accordingly, the approach to direction, supervision and review will vary from one engagement to the next, taking into account the nature and circumstances of the engagement. The approach will generally include a combination of addressing the firm's policies or procedures and engagement specific responses.

A79. The approach to the direction and supervision of the members of the engagement team and the review of their work provides support for the engagement partner in fulfilling the requirements of this ISA, and in concluding that the engagement partner has been sufficiently and appropriately involved throughout the audit engagement in accordance with paragraph 40.

A80. Ongoing discussion and communication among members of the engagement team allows less experienced engagement team members to raise questions with more experienced engagement

team members (including the engagement partner) in a timely manner and enables effective direction, supervision and review in accordance with paragraph 30(c).

Direction

A81. Direction of the engagement team may involve informing the members of the engagement team of their responsibilities, such as:

- Contributing to the management and achievement of quality at the engagement level through their personal conduct, communication and actions.
- Maintaining a questioning mind and being aware of unconscious or conscious auditor biases in exercising professional skepticism when gathering and evaluating audit evidence (see paragraph A37).
- Fulfilling relevant ethical requirements.
- The responsibilities of respective partners when more than one partner is involved in the conduct of an audit engagement.
- The responsibilities of respective engagement team members to perform audit procedures and of more experienced engagement team members to direct, supervise and review the work of less experienced engagement team members.
- Understanding the objectives of the work to be performed and the detailed instructions regarding the nature, timing and extent of planned audit procedures as set forth in the overall audit strategy and audit plan.
- Addressing threats to the achievement of quality, and the engagement team's expected response. For example, budget constraints or resource constraints should not result in the engagement team members modifying planned audit procedures or failing to perform planned audit procedures.

Supervision

A82. Supervision includes matters such as:

- Tracking the progress of the audit engagement, which includes monitoring:
 - The progress against the audit plan;
 - Whether the objective of work performed has been achieved; and
 - The ongoing adequacy of assigned resources.
- Taking appropriate action to address issues arising during the engagement, including for example, reassigning planned audit procedures to more experienced engagement team members when issues are more complex than initially anticipated.
- Addressing matters arising during the audit engagement, considering their significance and modifying the planned approach appropriately.
- Identifying matters for consultation or consideration by more experienced engagement team members during the audit engagement.

- Providing coaching and on-the-job training to help engagement team members develop skills or competencies.
- Creating an environment where engagement team members raise concerns without fear of reprisals.

Review

A83. Review of the engagement team's work provides support for the conclusion that the requirements of this ISA have been addressed.

A84. Review of the engagement team's work consists of consideration of whether, for example:

- The work has been performed in accordance with the firm's policies or procedures, professional standards and applicable law or regulation;
- Significant matters have been raised for further consideration;
- Appropriate consultations have taken place and the resulting conclusions have been documented and implemented;
- There is a need to revise the nature, timing and extent of work performed;
- The work performed supports the conclusions reached and is appropriately documented;
- The evidence obtained is sufficient and appropriate to support the auditor's report; and
- The objectives of the audit procedures have been achieved.

A85. The firm's policies or procedures may contain specific requirements regarding:

- The nature, timing and extent of review of audit documentation;
- Different types of review that may be appropriate in different situations (e.g., review of each individual working paper or selected working papers); and
- Which members of the engagement team are required to perform the different types of review.

The Engagement Partner's Review (Ref: Para. 31–34)

A86. As required by ISA 300, the engagement partner reviews the overall audit strategy and audit plan.³⁷ As required by ISA 230, the engagement partner documents the date and extent of the review.³⁸

A87. Timely review of documentation by the engagement partner at appropriate stages throughout the audit engagement enables significant matters to be resolved to the engagement partner's satisfaction on or before the date of the auditor's report. The engagement partner need not review all audit documentation.

A88. The engagement partner exercises professional judgment in identifying the areas of significant judgment made by the engagement team. The firm's policies or procedures may specify certain matters that are commonly expected to be significant judgments. Significant judgments in relation to the audit engagement may include matters related to the overall audit strategy and audit plan for

³⁷ ISA 300, paragraph 11A

³⁸ ISA 230, *Audit Documentation*, paragraph 9(c)

undertaking the engagement, the execution of the engagement and the overall conclusions reached by the engagement team, for example:

- Matters related to planning the engagement such as matters related to determining materiality.
- The composition of the engagement team, including:
 - Personnel using expertise in a specialized area of accounting or auditing;
 - The use of personnel from service delivery centers;
- The decision to involve an auditor's expert, including the decision to involve an external expert.
- The engagement team's consideration of risks identified through the acceptance and continuance process and proposed responses to those risks.
- The engagement team's risk assessment process, including situations where consideration of inherent risk factors and the assessment of inherent risk requires significant judgment by the engagement team.
- The engagement team's consideration of related party relationships and transactions and disclosures.
- Results of the procedures performed by the engagement team on significant areas of the engagement, for example, conclusions in respect of certain accounting estimates, accounting policies or going concern considerations.
- The engagement team's evaluation of the work performed by experts and conclusions drawn therefrom.
- In group audit situations:
 - The proposed overall group audit strategy and group audit plan, including the identification of significant components;
 - Decisions about the involvement of component auditors, including how to direct and supervise them and review their work. For example, if a component auditor is located in a jurisdiction or is from a firm with significant audit inspection findings, then judgments about their involvement in the engagement and the direction and supervision of component auditors and review of their work are likely to be more significant; and
 - The evaluation of work performed by component auditors and the conclusions drawn therefrom.
- How matters affecting the overall audit strategy and audit plan have been addressed.
- The significance and disposition of corrected and uncorrected misstatements identified during the engagement.
- The proposed audit opinion and matters to be communicated in the auditor's report, for example, key audit matters, or a "Material Uncertainty Related to Going Concern" paragraph.

A89. The engagement partner exercises professional judgment in determining other matters to review, for example based on:

- The nature and circumstances of the audit engagement.

- Which engagement team member performed the work.
- Matters relating to recent inspection findings.
- The requirements of the firm's policies or procedures.

Nature, Timing and Extent (Ref: Para. 30)

A90. The nature, timing and extent of the direction, supervision and review are required to be planned and performed in accordance with the firm's policies or procedures. For example, the firm may require that:

- Work planned to be performed at an interim date be directed, supervised and reviewed at the same time as the performance of the procedures rather than at the end of the period, so that any necessary corrective action can be taken in a timely manner.
- Certain matters are to be reviewed by the engagement partner and may specify the circumstances or engagements in which such matters are expected to be reviewed.

A91. The approach to direction, supervision and review may be tailored depending on, for example:

- The engagement team member's previous experience with the entity and the area to be audited. For example, if the work related to the entity's information system is being performed by the same engagement team member who performed the work in the prior period and there are no significant changes to the information system, the extent and frequency of the direction and supervision of the engagement team member may be less and the review of the related working papers may be less detailed.
- The complexity of the entity. For example, if significant events have occurred at the entity or in the industry in which the entity operates since the previous audit engagement or during the current engagement, the extent and frequency of the direction and supervision of the engagement team member may be greater and the review of the related working papers may be more detailed.
- The assessed risks of material misstatement. For example, a higher assessed risk of material misstatement may require a corresponding increase in the extent and frequency of the direction and supervision of engagement team members and a more detailed review of their work.
- The competence and capabilities of the individual engagement team members performing the audit work. For example, less experienced engagement team members may require more detailed instructions and more frequent, or in-person, interactions as the work is performed.
- The manner in which the reviews of the work performed are expected to take place. For example, in some circumstances, remote reviews may not be effective in providing the necessary direction and may need to be supplemented by in-person interactions.
- The structure of the engagement team and the location of engagement team members, including when auditors from outside the firm's network or service delivery centers are used. For example, direction and supervision of individuals located at service delivery centers and the review of their work may need to be more formalized and structured than when members of the engagement team are all situated in the same location.

- A92. Identification of changes in the engagement circumstances may warrant reevaluation of the planned approach to the nature, timing or extent of direction, supervision or review. For example, if the assessed risk at the financial statement level increases because of a complex transaction, the engagement partner may need to change the planned level of review of the work related to the transaction.
- A93. In accordance with paragraph 30(b), the engagement partner is required to determine that the approach to direction, supervision and review is responsive to the nature and circumstances of the audit engagement. For example, if a more experienced engagement team member becomes unavailable to participate in the supervision and review of the engagement team, the engagement partner may need to increase the extent of supervision and review of the less experienced engagement team members.

Review of Communications to Management, Those Charged with Governance, or Regulatory Authorities
(Ref: Para. 34)

- A94. The engagement partner may exercise professional judgment in determining which formal written communications to review, taking into account the nature and circumstances of the audit engagement. For example, it may not be necessary for the engagement partner to review communications between the engagement team and management in the ordinary course of the audit.

Consultation (Ref: Para. 35)

- A95. Proposed ISQM 1 requires the firm to establish policies or procedures addressing consultation on difficult or contentious matters, including the engagement team's responsibilities for consultation, the matters on which to consult, and how the conclusions should be agreed and implemented. Consultation may be appropriate or required, for example for:

- Issues that are complex or unfamiliar (e.g., issues related to an accounting estimate with a high degree of estimation uncertainty);
- Significant risks;
- Significant transactions that are outside the normal course of business for the entity, or that otherwise appear to be unusual;
- Limitations imposed by management; and
- Non-compliance with law or regulation.

- A96. Effective consultation on significant technical, ethical and other matters within the firm or, where applicable, outside the firm may be achieved when those consulted:

- Are given all the relevant facts that will enable them to provide informed advice; and
- Have appropriate knowledge, seniority and experience.

- A97. It may be appropriate for the engagement team, in the context of the firm's policies or procedures, to consult outside the firm, for example, where the firm lacks appropriate internal resources. The engagement team may take advantage of advisory services provided by firms, professional and regulatory bodies or commercial organizations that provide relevant quality control services.

A98. The need for consultation outside the engagement team on a difficult or contentious matter may be an indicator that the matter is a key audit matter.³⁹

Engagement Quality Review (Ref: Para. 36)

A99. Proposed ISQM 1 requires that the firm establish policies or procedures that require an engagement quality review for certain types of engagements.⁴⁰ Proposed ISQM 2⁴¹ deals with the appointment and eligibility of the engagement quality reviewer and the engagement quality reviewer's responsibilities relating to performing and documenting an engagement quality review.

Completion of the Engagement Quality Review Before Dating of the Auditor's Report (Ref: Para. 36(d))

A100. ISA 700 (Revised) requires the auditor's report to be dated no earlier than the date on which the auditor has obtained sufficient appropriate audit evidence on which to base the auditor's opinion on the financial statements.⁴² If applicable to the audit engagement, [proposed] ISQM 2 requires that the engagement quality review be completed on or before the date of the auditor's report.

A101. The auditor's report cannot be dated until the completion of the engagement quality review. For example, if the engagement quality reviewer has communicated to the engagement partner concerns about the significant judgments made by the engagement team or that the conclusions reached thereon were not appropriate then the engagement quality review is not complete.⁴³

A102. An engagement quality review that is conducted in a timely manner at appropriate stages during the audit engagement may assist the engagement team in promptly resolving matters raised to the engagement quality reviewer's satisfaction on or before the date of the auditor's report.

A103. Frequent communications between the engagement team and the engagement quality reviewer throughout the audit engagement may assist in facilitating an effective and timely engagement quality review. In addition to discussing significant matters with the engagement quality reviewer, the engagement partner may assign responsibility for coordinating requests from the engagement quality reviewer to another member of the engagement team.

Differences of Opinion (Ref: Para. 37–38)

A104. Proposed ISQM 1 sets out requirements for the firm to establish policies or procedures to address differences of opinion that arise within the engagement team, or between the engagement team and the engagement quality reviewer or personnel performing activities within the firm's system of quality management, including those who provide consultation.

A105. In some circumstances, the engagement partner may not be satisfied with the resolution of the difference of opinion. In such circumstances, appropriate actions for the engagement partner may include, for example:

- Seeking legal advice; or

³⁹ ISA 701, paragraphs 9 and A15

⁴⁰ [Proposed] ISQM 1, paragraph 41A(c)

⁴¹ Proposed ISQM 2, *Engagement Quality Reviews*

⁴² ISA 700 (Revised), paragraph 49

⁴³ Proposed ISQM 2, paragraph 21(b)

- Withdrawing from the audit engagement, when withdrawal is possible under applicable law or regulation.

Monitoring and Remediation (Ref: Para. 39)

A106. Under [proposed] ISQM 1, the firm is required to establish quality objectives and responses to address the firm's monitoring and remediation process that enable the evaluation of the design, implementation and operation of the components of the system of quality management and whether the quality objectives have been achieved. In addition, the firm is required to communicate to personnel information about the firm's monitoring and remediation process to the extent that it is relevant to their responsibilities and to enable the personnel to take prompt and appropriate action in accordance with their responsibilities. The results of the firm's monitoring and remediation activities are based on an evaluation of findings from the firm's monitoring activities, the results of external inspections and other relevant information that the firm obtains or of which the firm becomes aware. Information provided by members of the engagement team to the firm is part of the other relevant information for the firm's monitoring and remediation process, and exercising professional judgment and professional skepticism while conducting the audit may assist the auditor in remaining alert for information that may be relevant to that process.

A107. Information provided by the firm may be relevant to the audit engagement when, for example, it relates to findings identified on another engagement performed by the engagement partner or other members of the engagement team, findings from the local firm office or previous inspection results of audits of the entity.

A108. In considering relevant information communicated by the firm through its monitoring and remediation process and how it may affect the audit engagement, the engagement partner may consider the remedial actions designed and implemented by the firm to deal with identified deficiencies and, to the extent relevant to the nature and circumstances of the engagement, communicate accordingly to the engagement team. The engagement partner may also determine whether additional remedial actions are needed at the engagement level. For example, the engagement partner may determine that:

- An auditor's expert should be used; or
- The nature, timing and extent of direction, supervision and review needs to be enhanced in an area of the audit where deficiencies have been identified.

If an identified deficiency does not affect the quality of the audit (e.g., if it relates to a technological resource that the engagement team did not use) then no further action may be needed.

A109. A deficiency in the firm's system of quality management does not necessarily indicate that an audit engagement was not performed in accordance with professional standards and applicable legal and regulatory requirements, or that the auditor's report was not appropriate in the circumstances.

Taking Overall Responsibility for Managing and Achieving Quality (Ref: Para. 40)

A110. Under [proposed] ISQM 1, the firm is required to establish objectives relating to the engagement partner's overall responsibility for managing and achieving quality on the engagement and for being sufficiently and appropriately involved throughout the audit engagement.

A111. Relevant considerations in addressing the requirement in paragraph 40 include determining how the engagement partner has complied with the requirements of this ISA, given the nature and

circumstances of the audit engagement and how the audit documentation evidences the engagement partner's involvement throughout the audit engagement, as described in paragraph A114.

A112. If the engagement partner's involvement does not provide the basis for determining that the significant judgments made and the conclusions reached are appropriate, the engagement partner will not be able to reach the determination required by paragraph 40. In addition to taking account of firm policies or procedures that may set forth the required actions to be taken in such circumstances, appropriate actions that the engagement partner may take, include, for example:

- Reevaluating the planned approach to the nature and extent of review and modifying the planned approach to increase the involvement of the engagement partner; or
- Consulting with firm personnel assigned operational responsibility for the relevant aspect of the firm's system of quality management.

Documentation (Ref: Para. 41)

A113. In accordance with ISA 230,⁴⁴ 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.

A114. Documentation of the performance of the requirements of this ISA, including evidencing the involvement of the engagement partner and the engagement partner's determination in accordance with paragraph 40, may be accomplished in different ways depending on the nature and circumstances of the audit engagement. For example:

- Direction of the engagement team can be documented through signoffs of the audit plan and project management activities;
- Minutes from meetings of the engagement team may provide evidence of the clarity, consistency and effectiveness of the engagement partner's communications and other actions in respect of culture and expected behaviors that reflect the firm's commitment to quality;
- Agendas from discussions between the engagement partner and other members of the engagement team, and where applicable the engagement quality reviewer, and related signoffs and records of the time the engagement partner spent on the engagement, may provide evidence of the engagement partner's involvement throughout the audit engagement and supervision of other members of the engagement team; and
- Signoffs by the engagement partner and other members of the engagement team provide evidence that the working papers were reviewed.

A115. When dealing with circumstances that may pose risks to achieving quality on the audit engagement, the exercise of professional skepticism, and the documentation of the auditor's consideration thereof, may be important. For example, if the engagement partner obtains information that may have caused the firm to decline the engagement (see paragraph 24), the documentation may include explanations of how the engagement team dealt with the circumstance.

⁴⁴ ISA 230, paragraph A7

A116. Documentation of consultations with other professionals that involve difficult or contentious matters that is sufficiently complete and detailed contributes to an understanding of:

- The nature and scope of the issue on which consultation was sought; and
- The results of the consultation, including any decisions taken, the basis for those decisions and how they were implemented.