

**Exposure Drafts**  
**February 2019**

*Comments due: July 1, 2019*

The IAASB's Exposure Drafts  
for Quality Management at the  
Firm and Engagement Level,  
Including Engagement Quality  
Reviews

**IAASB**

International Auditing  
and Assurance  
Standards Board

## **About the IAASB**

This Exposure Draft was developed and approved by the International Auditing and Assurance Standards Board (IAASB).

The objective of the IAASB is to serve the public interest by setting high-quality auditing, assurance, and other related standards and by facilitating the convergence of international and national auditing and assurance standards, thereby enhancing the quality and consistency of practice throughout the world and strengthening public confidence in the global auditing and assurance profession.

The IAASB develops auditing and assurance standards and guidance for use by all professional accountants under a shared standard-setting process involving the Public Interest Oversight Board, which oversees the activities of the IAASB, and the IAASB Consultative Advisory Group, which provides public interest input into the development of the standards and guidance. The structures and processes that support the operations of the IAASB are facilitated by the International Federation of Accountants (IFAC).

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## REQUEST FOR COMMENTS

This Explanatory Memorandum, *The IAASB's Exposure Drafts for Quality Management at the Firm and Engagement Level, Including Engagement Quality Reviews*, was developed and approved by the International Auditing and Assurance Standards Board® (IAASB®).

The proposals in this Explanatory Memorandum may be modified in light of comments received before being issued in final form. **Comments are requested by July 1, 2019.**

Respondents are asked to submit their comments electronically through the IAASB website, using the "[Submit a Comment](#)" link. Please submit comments in both a PDF and Word file. First-time users must register to use this feature. All comments will be considered a matter of public record and will ultimately be posted on the website.

This publication may be downloaded from the IAASB website: <http://www.iaasb.org>. The approved text is published in the English language.

**THE IAASB’S EXPOSURE DRAFTS FOR QUALITY MANAGEMENT AT  
THE FIRM AND ENGAGEMENT LEVEL, INCLUDING ENGAGEMENT  
QUALITY REVIEWS**

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## Section 1 Introduction

1. This memorandum provides background to the IAASB's three Exposure Drafts for quality management at the firm and engagement levels:
  - (a) Proposed International Standard on Quality Management 1 (Previously International Standard on Quality Control (ISQC) 1<sup>1</sup>), *Quality Management for Firms that Perform Audits or Reviews of Financial Statements, or Other Assurance or Related Services Engagements* (ED-ISQM 1).
  - (b) Proposed International Standard on Quality Management 2, *Engagement Quality Reviews* (ED-ISQM 2).
  - (c) Proposed International Standard on Auditing 220 (Revised), *Quality Management for an Audit of Financial Statements* (ED-220).

The three proposed standards were approved for exposure by the IAASB in December 2018. The IAASB is of the view that the three standards will, individually and collectively, improve the quality of engagements through addressing key public interest issues related to the management of quality at a firm and engagement level and the performance of engagement quality reviews.

2. This memorandum also provides an explanation of the significant issues pervasive to the three exposure drafts, including a discussion of scalability and the interrelationship of the three proposed standards. It also sets out the IAASB's proposals regarding the effective date and the related implementation period for the three proposed standards, as well as the IAASB's planned implementation support activities.
3. This memorandum should be read in conjunction with the explanatory memorandums for each of the three proposed standards, which provide background to each of the exposure drafts, and the key issues considered by the IAASB in developing the exposure drafts. The explanatory memorandums for each of the standards are available at <http://www.iaasb.org/quality-management>.

### Section 1-A – Background

4. In March 2009, the IAASB completed its Clarity Project, designed to improve the clarity and understandability of the International Standards on Auditing (ISAs) and ISQC 1. Firms were required to establish a system of quality control in compliance with extant ISQC 1 by December 15, 2009. At the engagement level, extant ISA 220<sup>2</sup> was effective for audits of financial statements for periods beginning on or after December 15, 2009. Requirements and application material on engagement quality control reviews were included in both ISQC 1 and ISA 220. Following the completion of the Clarity Project, the IAASB developed its Strategy and Work Program for 2009-2011. One of the initiatives in the IAASB's Strategy and Work Program 2009–2011 was the development of a process for assessing the effectiveness of the implementation of the clarified ISAs, including ISQC 1 and ISA 220.
5. The post-implementation review of the clarified ISAs was completed in 2013, and the [findings](#) from this review formed the basis for the [IAASB's Strategy for 2015–2019](#) and the [IAASB Work Plan for 2015–2016: Enhancing Audit Quality and Preparing for the Future](#). Findings with regard to ISQC 1

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<sup>1</sup> ISQC 1, *Quality Control for Firms that Perform Audits and Reviews of Financial Statements, and Other Assurance and Related Services Engagements*

<sup>2</sup> ISA 220, *Quality Control for an Audit of Financial Statements*

and ISA 220 suggested that additional guidance was needed to demonstrate how ISQC 1 could be applied proportionately by small- and medium-sized practitioners (SMPs) and that there were calls to make various aspects of the standards more robust. Accordingly, the Board included planned work on its quality control standards in its Strategy for 2015–2019 and its Work Plan for 2015–2016.

6. As work commenced on the IAASB's quality control standards, the working groups reflected on the issues identified through the post-implementation review of the clarified ISAs, inspection findings and ongoing outreach. The IAASB released the Invitation to Comment (ITC), [\*Enhancing Audit Quality: A Focus on Professional Skepticism, Quality Control and Group Audits\*](#), in December 2015 to obtain stakeholder views on key issues regarding quality control, group audits, and professional skepticism. Respondents generally agreed that the IAASB should take action to address the issues presented in the ITC.
7. Recognizing the importance of taking action to respond to the issues identified, in December 2016 the IAASB approved the [project](#) to revise ISQC 1 and ISA 220 and develop other outputs, as necessary. The project proposal included engagement quality reviews as one of the issues to be addressed.

### **Section 1-B – Key Public Interest Issues**

8. The proposed revisions in ED-ISQM 1, ED-ISQM 2 and ED-220 have been made with the public interest at the forefront. The proposed revisions address the most relevant public interest issues related to quality control, including the following issues that were identified in the ITC:
  - (a) Fostering an appropriately independent and challenging skeptical mindset of the auditor.
  - (b) Encouraging proactive quality management at the firm and engagement level.
  - (c) Exploring transparency and its role in audit quality.
  - (d) Focusing more on firms' (including networks') structures and communication processes and their internal and external monitoring and remediation activities.
  - (e) Reinforcing the need for robust communication and interactions during the audit engagement.
9. The explanatory memorandums for each of the standards further explain how the above public interest issues have been addressed.

## **Section 2 Significant Matters**

### **Section 2-A – Scalability of the Standards and a New Approach to Quality Management**

10. The business environment is becoming increasingly complex; expectations of firms' stakeholders are escalating and there is growing pressure for the IAASB's standards to keep pace with these changes to enhance engagement quality. These factors have given rise to challenges in developing international standards that enhance engagement quality and address complex issues. Developing standards in this environment may lead to more detailed and longer standards, but at the same time the IAASB is conscious that the standards need to be able to be effectively applied to a wide range of circumstances, including, in particular, audits of less complex entities. Addressing the scalability of the IAASB's International Standards is a key focus area for the IAASB to make sure that the standards are scalable to all types of engagements. The IAASB is also aware of the need for its standards to be fit-for-purpose for all firms, regardless of their size or complexity.

11. In order to improve the robustness of firms' systems of quality control and address the scalability of extant ISQC 1, the ITC proposed a new approach that encourages proactive management of quality. This approach is intended to be adaptable to the size and nature of a firm or the services it provides. Taking into account the ITC respondents' views on the proposed new approach, the IAASB concluded that ED-ISQM 1 should adopt the new approach, termed quality management, that is focused on how each firm manages its risks to quality. The explanatory memorandum for ED-ISQM 1 provides further explanation of this approach and the IAASB's key considerations in incorporating it into ED-ISQM 1. ED-220 takes this further by embedding the principles of quality management into the engagement level requirements. The explanatory memorandum for ED-ISQM 1 explains that the references to "quality control" have been changed to "quality management." The new terms have also been used in ED-ISQM 2 and ED-220.
12. In addition to the new quality management approach, the IAASB has taken various other steps to address scalability across the standards, which have been further discussed in the explanatory memorandums for each of the standards. In particular, ED-ISQM 1 emphasizes the need for the firm to consider the nature and circumstances of the firm and the engagements it performs in designing, implementing and operating its system of quality management, and the standard is focused on achieving quality objectives that are outcomes-based. Similarly, ED-220 has increased the focus on taking into account the nature and circumstances of the audit engagement in managing quality at the engagement level.
13. Given the importance of the scalability of the IAASB's International Standards, the IAASB is seeking input from respondents, in particular SMPs, on the scalability of each of the standards.

## **Section 2-B – Interrelationship between the Standards**

### *Relationship Between Quality Management at the Firm and the Engagement Level*

14. Although a new quality management approach has been introduced in ED-ISQM 1, the nature and spirit of the relationship between ED-220 and ED-ISQM 1 has not changed. The firm is responsible for establishing its system of quality management, which provides the foundation for managing quality at the engagement level, and the engagement partner is responsible for managing and achieving quality at the engagement level.
15. Although the firm is responsible for establishing its system of quality management, aspects of the system of quality management may be implemented at the engagement level, as illustrated in paragraph A62 of ED-ISQM 1. The extent to which aspects of the firm's system of quality management are implemented at the engagement level will depend on the nature and circumstances of the firm and the engagements it performs. For example, in the case of a sole practitioner, it is possible that much of the firm's system of quality management will operate at the engagement level.
16. Various enhancements have been made to ED-ISQM 1 and ED-220 to clarify the respective responsibilities of the firm and the engagement partner. These include:
  - (a) A new requirement in paragraph 41(b) of ED-ISQM 1 for the firm to communicate the responsibility for implementing the firm's responses to relevant personnel, including engagement teams.
  - (b) An explicit statement in paragraph 4 of ED-220 regarding the responsibility of the engagement team, led by the engagement partner, for implementing the firm's responses to quality risks that are applicable to the audit engagement. This paragraph also explains the engagement

partner's further responsibilities for determining whether to design and implement responses beyond those required by the firm, given the nature and circumstances of the engagement. This is intended to recognize that the firm cannot identify and design and implement responses to address all quality risks that are relevant to the engagement.

#### *Two-Way Communication*

17. As highlighted in Section 1–B, one of the most significant public interest issues highlighted in the ITC was reinforcing the need for robust communication and interactions during the audit. Ongoing communication between the firm, its engagement quality reviewers and its engagement teams is necessary for the firm's system of quality management to operate effectively and to support the performance of engagements. The IAASB is of the view the importance of this communication should be emphasized and therefore ED-ISQM 1, ED-ISQM 2 and ED-220 now include various requirements and application material that address the required communications between the various parties.

#### *A New Standard for Engagement Quality Reviews*

18. Given the importance and value placed on the role of the engagement quality review by stakeholders, particularly investors and regulators, it was proposed in the ITC that a separate standard be developed for engagement quality reviews. The ITC further explained that doing so may help to address scalability and may provide a simpler mechanism for elaborating the requirements and application material for engagement quality reviews. Respondents to the ITC had mixed views about whether a separate standard for engagement quality reviews would be appropriate.
19. As the IAASB's thinking about the new quality management approach evolved and the revisions to ED-ISQM 1 progressed and as the work advanced on addressing issues relating to engagement quality reviews, the IAASB concluded that it would be better to place the more detailed requirements and related application material for engagement quality reviews in a separate standard, ED-ISQM 2. The explanatory memorandum for ED-ISQM 2 provides further information regarding the IAASB's key considerations in determining that a separate standard should be developed for engagement quality reviews, including how the requirements between ED-ISQM 1 and ED-ISQM 2 have been linked.
20. As a result of the development of a separate standard for engagement quality reviews, the requirements in extant ISA 220 dealing with the responsibilities of the engagement quality control reviewer have been removed from ED-220, and revised and relocated to ED-ISQM 2. The IAASB noted that this approach reinforces the function of the engagement quality review as a firm-level activity that is undertaken by an individual who is acting on behalf of the firm, and results in ISA 220-ED dealing with the responsibilities of the engagement team, including the engagement partner, in relation to managing and achieving quality at the engagement level.

### **Section 3 Effective Date**

21. In finalizing the three standards, the IAASB considered the possible effective dates for each of the standards, recognizing that the effective dates would need to be aligned because of the interrelationships of the standards described previously in this memorandum. The IAASB also considered the appropriate wording of the effective dates of the standards, in particular ED-ISQM 2 given that the standard addresses all types of engagements and some engagements do not relate to a particular period. The proposed wording of the effective date paragraphs are included in each of



the standards (see paragraph 17 of ED-ISQM 1, paragraph 9 of ED-ISQM 2 and paragraph 8 of ED-220).

22. The IAASB is proposing that an implementation period of approximately 18 months following the approval of the standards by the Public Interest Oversight Board,<sup>3</sup> would be appropriate for all three proposed standards.
23. In proposing these effective dates, the IAASB noted the concerns of stakeholders that firms' systems of quality control and the management of engagement quality is an area requiring urgent improvement. For example, the [International Forum of Independent Audit Regulators' 2017 Inspection Findings Survey](#) highlights that findings related to firms' systems of quality control continue to occur and that improvements are needed. The IAASB is of the view that the three standards will, individually and collectively, improve the quality of engagements through addressing the key public interest issues mentioned previously in this document. Accordingly, facilitating timely and effective implementation of the three standards such that the intended benefits are realized, is a priority of the IAASB and in the public interest.
24. Establishing an implementation period that allows enough time to effectively implement the standards, including the translation of the standards and the development of implementation guidance and support materials, is important. The new quality management approach in ED-ISQM 1 represents a substantial revision to the extant standard and there are various other new requirements across the three standards that enhance the rigor of the standards. Accordingly, there will be a need for focused and likely substantial effort by firms and engagement teams to implement the new standards. For example, unlike extant ISQC 1 that sets forth discrete requirements for matters that the firm's policies and procedures are required to address, the new quality management approach requires firms to design, implement and operate an integrated system of quality management, including (1) identifying and assessing their quality risks, (2) designing and implementing responses to address the assessed quality risks, and (3) designing processes related to monitoring and remediation. Designing and implementing the new system of quality management will take time and effort and increased levels of coordination and cooperation within the firm, and may also require internal organizational changes and the acquisition and development of resources. For firms that belong to a network, there will be a direct impact on the network given the need for increased cooperation between the firm and the network and a likely desire by some networks for centralized implementation efforts to support the implementation at a member firm level and to improve the consistency and quality of the implementation. Furthermore, firms or networks will likely need time to test aspects of the system to determine that they are appropriate for use across the firm or the network before implementing them. There may also be firms, including SMPs, who will be dependent on guidance and support materials developed by national standard setters or professional accounting organizations to implement the standards.
25. Bearing in mind the perspectives outlined in paragraphs 23–24 above, the IAASB concluded that proposing an 18 month implementation period, supported by appropriate implementation support materials, is both practical and in the public interest. The IAASB notes that a rushed implementation may exacerbate risks to quality, lead to increased inspection findings, and would be inconsistent with

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<sup>3</sup> When the final standards are approved by the IAASB, their approval is subject to the approval of the Public Interest Oversight Board that an appropriate due process was followed. Typically, the Public Interest Oversight Board approves the standards one quarter after the approval of the standards by the IAASB. For example, if the standards are approved by the IAASB in March 2020, the approval of the Public Interest Oversight Board is likely to be sought in June 2020.

the objectives of the IAASB's project to enhance its quality management standards. Accordingly, the IAASB is interested in respondents' views about whether an 18 month implementation period is appropriate (see question 1).

26. The IAASB proposes to allow early adoption; however, all three standards would need to be early adopted as a package due to the linkages between them and the incompatibility with extant standards that would result from selective early adoption of only one or two of the new standards.

## Section 4 Conforming Amendments

27. As a result of the proposals in the three EDs, the IAASB is also proposing conforming amendments to the following IAASB pronouncements: the *Preface to the International Quality Management, Auditing, Review, Other Assurance, and Related Services Pronouncements*; ISA 200;<sup>4</sup> ISA 210;<sup>5</sup> ISA 230;<sup>6</sup> ISA 250 (Revised);<sup>7</sup> ISA 260 (Revised);<sup>8</sup> ISA 300;<sup>9</sup> ISA 500;<sup>10</sup> ISA 540 (Revised);<sup>11</sup> ISA 610 (Revised 2013);<sup>12</sup> ISA 620;<sup>13</sup> ISA 700 (Revised);<sup>14</sup> ISA 701;<sup>15</sup> ISA 720 (Revised);<sup>16</sup> and IAPN 1000.<sup>17</sup>
28. These conforming amendments are included in the Appendix. The conforming amendments do not include:
- Changes for the revised and restructured International Ethics Standards Board for Accountants (IESBA) *International Code of Ethics for Professional Accountants (including International Independence Standards)*; and
  - Conforming and consequential amendments to the assurance and related services standards arising from the quality management standards.

Separate projects will be considered in 2019 to determine the nature and scope of necessary amendments or changes for these matters.

## Section 5 Perspectives on Practical Implementation

29. For most firms, the proposals would result in a significant change in practice, in particular the proposals in ED-ISQM 1. The nature and extent of change would however depend on many factors,

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<sup>4</sup> ISA 200, *Overall Objectives of the Independent Auditor and the Conduct of an Audit in Accordance With International Standards on Auditing*

<sup>5</sup> ISA 210, *Agreeing the Terms of Audit Engagements*

<sup>6</sup> ISA 230, *Audit Documentation*

<sup>7</sup> ISA 250 (Revised), *Consideration of Laws and Regulations in an Audit of Financial Statements*

<sup>8</sup> ISA 260 (Revised), *Communication with Those Charged with Governance*

<sup>9</sup> ISA 300, *Planning an Audit of Financial Statements*

<sup>10</sup> ISA 500, *Audit Evidence*

<sup>11</sup> ISA 540 (Revised), *Auditing Accounting Estimates and Related Disclosures*

<sup>12</sup> ISA 610 (Revised 2013), *Using the Work of Internal Auditors*

<sup>13</sup> ISA 620, *Using the Work of an Auditor's Expert*

<sup>14</sup> ISA 700 (Revised), *Forming an Opinion and Reporting on Financial Statements*

<sup>15</sup> ISA 701, *Communicating Key Audit Matters in the Independent Auditor's Report*

<sup>16</sup> ISA 720 (Revised), *The Auditor's Responsibilities Relating to Other Information*

<sup>17</sup> IAPN 1000, *Special Considerations in Auditing Financial Instruments*

such as the nature and circumstances of the firm and the engagements the firm performs, and the extent to which the firm already uses a risk-based approach in managing quality. The IAASB is aware that some firms have already evolved their processes to incorporate a risk-based approach to quality management, and that some have also commenced activities to plan for the implementation of the standards when they are eventually issued. The IAASB is interested in learning about practical challenges and experiences in implementing the proposals and the possible effects of the proposals. This includes the perspectives of SMPs regarding any practical challenges that can be foreseen in implementing the standards.

## Section 6 Implementation Support

30. The IAASB is currently in the [process of developing its strategy for 2020–2023](#), with an increased focus on other mechanisms for addressing issues and challenges on a more timely basis, including implementation support that is of particular importance to SMPs. Recognizing the increasing demand for implementation support, the IAASB plans to develop materials to accompany the standards, in particular ED-ISQM 1, to facilitate an improved understanding of the standards. The IAASB has developed illustrations of the accompanying materials to facilitate input from respondents on the nature of implementation support that is most useful. The illustrative materials include:
- (a) Practical examples that demonstrate how the requirements of ED-ISQM 1 may be scaled according to the nature and circumstances of the firm and its engagements.
  - (b) Frequently asked questions that provide additional explanations and examples of more complex aspects of ED-ISQM 1.
31. In addition, during the exposure period, the IAASB plans to undertake various outreach activities, such as videos and webcasts, that will also provide a mechanism for respondents to further understand the standards, in particular their application to SMPs.

## Section 7 Request for Comments

The explanatory memorandums for each of the standards include questions about the key issues considered by the IAASB in developing the exposure drafts, and are available at [www.iaasb.org/quality-management](http://www.iaasb.org/quality-management). The questions below address key issues pervasive to the three standards. Comments will be most helpful if they include the reasons for any concern about the matters covered in the questions below.

### Overall Questions

- 1) Do you support the approach and rationale for the proposed implementation period of approximately 18 months after the approval of the three standards by the Public Interest Oversight Board? If not, what is an appropriate implementation period?
- 2) In order to support implementation of the standards in accordance with the IAASB's proposed effective date, what implementation materials would be most helpful, in particular for SMPs?

### General Questions

In addition, the IAASB is also seeking comments on the general matters set out below for all three EDs:

- (a) *Developing Nations*—Recognizing that many developing nations have adopted or are in the process of adopting the International Standards, the IAASB invites respondents from these nations to

comment on the proposals, in particular, on any foreseeable difficulties in applying it in a developing nation environment.

- (b) *Public Sector*—The IAASB welcomes input from public sector auditors on how the proposed standards affect engagements in the public sector, particularly regarding whether there are potential concerns about the applicability of the proposals to the structure and governance arrangements of public sector auditors.
- (c) *Translations*—Recognizing that many respondents may intend to translate the final ISQMs and ISA for adoption in their own environments, the IAASB welcomes comment on potential translation issues respondents may note in reviewing the proposed standards.

**PROPOSED CONFORMING AMENDMENTS TO THE INTERNATIONAL STANDARDS ON AUDITING ARISING FROM PROPOSED INTERNATIONAL STANDARD ON QUALITY MANAGEMENT 1 AND INTERNATIONAL STANDARD ON AUDITING 220 (REVISED)**

***Preface to the International Quality ~~Control~~Management, Auditing, Review, Other Assurance, and Related Services Pronouncements***

**Introduction**

1. This preface to the *International Quality ~~Control~~Management, Auditing, Review, Other Assurance, and Related Services Pronouncements* is issued to facilitate understanding of the scope and authority of the pronouncements the International Auditing and Assurance Standards Board (IAASB) issues, as set forth in the IAASB's Terms of Reference.

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**The Authority Attaching to International Standards Issued by the International Auditing and Assurance Standards Board**

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10. International Standards on Quality ~~Control~~Management (ISQCMs) are to be applied for all services falling under the IAASB's Engagement Standards.

...

**International Standards on Quality ~~Control~~Management**

12. ISQCMs are written to apply to firms in respect of all their services falling under the IAASB's Engagement Standards. The authority of ISQCMs is set out in the introduction to ~~the~~each ISQCM.<sup>18</sup>

...

**Applicability of the International Standards**

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19. International Standards are relevant to engagements in the public sector. When appropriate, additional considerations specific to public sector entities are included:
  - (a) Within the body of an International Standard in the case of ISAs and ISQCMs; or
  - (b) In a Public Sector Perspective (PSP) appearing at the end of other International Standards. ...

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<sup>18</sup> Proposed ISQM 1, *Quality Management for Firms that Perform Audits or Reviews of Financial Statements, or Other Assurance or Related Services Engagements*, paragraph 16

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## **ISA 200, Overall Objectives of the Independent Auditor and the Conduct of an Audit in Accordance with International Standards on Auditing**

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### **Requirements**

#### **Ethical Requirements Relating to an Audit of Financial Statements**

14. The auditor shall comply with relevant ethical requirements, including those ~~pertaining~~related to independence, relating to financial statement audit engagements. (Ref: Para. A16–A19)

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### **Application and Other Explanatory Material**

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### **Definitions**

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#### **Ethical Requirements Relating to an Audit of Financial Statements (Ref: Para. 14)**

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- A19. International Standard on Quality Control~~Management~~ (ISQCM) 1,<sup>49</sup> or national requirements that are at least as demanding,<sup>20</sup> deal with the firm's responsibilities to ~~establish~~design, implement and maintain its operate a system of quality control for audit engagements. ISQC 1 sets out the responsibilities of management that provides the firm for ~~establishing policies and procedures designed to provide it with~~ reasonable assurance that the firm and its personnel ~~comply~~fulfill their responsibilities in accordance with professional standards and applicable legal and regulatory requirements, and conduct engagements in accordance with such standards and requirements. As part of its system of quality management, ISQM 1 requires the firm to address the fulfillment of responsibilities in accordance with relevant ethical requirements, including those pertainingrelated to independence.<sup>21</sup> ISA 220 (Revised) sets out the engagement partner's responsibilities with respect to relevant ethical requirements, including those related to independence.<sup>22</sup> ~~These include remaining alert, through observation and making inquiries as necessary, for evidence of non-compliance with relevant ethical requirements by members of the engagement team, determining the appropriate action if matters come to the engagement partner's attention that indicate that members of the engagement team have not complied with relevant ethical requirements, and forming a conclusion on compliance with independence requirements that apply to the audit engagement.~~<sup>23</sup> ISA 220

<sup>49</sup> ISQC 1, *Quality Control for Firms that Perform Audits and Reviews of Financial Statements, and Other Assurance and Related Services Engagements*

<sup>20</sup> ISA 220 (Revised), *Quality Control~~Management~~ for an Audit of Financial Statements*, paragraph 23

<sup>21</sup> ISQCM 1, paragraphs 20–25~~32–33~~

<sup>22</sup> ISA 220 (Revised), paragraphs 14–19

<sup>23</sup> ISA 220, paragraphs 9–12

~~recognizes that the engagement team is entitled to rely on a firm's system of quality control in meeting its responsibilities with respect to quality control procedures applicable to the individual audit engagement, unless information provided by the firm or other parties suggests otherwise.~~

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### **Professional Judgment** (Ref: Para. 16)

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A27. The exercise of professional judgment in any particular case is based on the facts and circumstances that are known by the auditor. Consultation on difficult or contentious matters during the course of the audit, both within the engagement team and between the engagement team and others at the appropriate level within or outside the firm, such as that required by ISA 220 (Revised),<sup>24</sup> assist the auditor in making informed and reasonable judgments.

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### **Sufficient Appropriate Audit Evidence and Audit Risk** (Ref: Para. 5 and 17)

#### *Sufficiency and Appropriateness of Audit Evidence*

A30. Audit evidence is necessary to support the auditor's opinion and report. It is cumulative in nature and is primarily obtained from audit procedures performed during the course of the audit. It may, however, also include information obtained from other sources such as previous audits (provided the auditor has determined whether changes have occurred since the previous audit that may affect its relevance to the current audit<sup>25</sup>) or through the information obtained by the firm in the acceptance or continuance of the client relationship or engagement~~firm's quality control procedures for client acceptance or continuance~~. In addition to other sources inside and outside the entity, the entity's accounting records are an important source of audit evidence. Also, information that may be used as audit evidence may have been prepared by an expert employed or engaged by the entity. Audit evidence comprises both information that supports and corroborates management's assertions, and any information that contradicts such assertions. In addition, in some cases, the absence of information (for example, management's refusal to provide a requested representation) is used by the auditor, and therefore, also constitutes audit evidence. Most of the auditor's work in forming the auditor's opinion consists of obtaining and evaluating audit evidence.

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### **Conduct of an Audit in Accordance with ISAs**

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#### *Contents of the ISAs* (Ref: Para. 19)

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<sup>24</sup> ISA 220 (Revised), paragraph 18~~32~~

<sup>25</sup> ISA 315 (Revised), *Identifying and Assessing the Risks of Material Misstatement through Understanding the Entity and Its Environment*, paragraph 9

A64. An ISA may include, in a separate section under the heading “Definitions,” a description of the meanings attributed to certain terms for purposes of the ISAs. These are provided to assist in the consistent application and interpretation of the ISAs, and are not intended to override definitions that may be established for other purposes, whether in law, regulation or otherwise. Unless otherwise indicated, those terms will carry the same meanings throughout the ISAs. The Glossary of Terms relating to International Standards issued by the International Auditing and Assurance Standards Board in the *Handbook of International Quality ~~Control~~ Management, Auditing, Review, Other Assurance, and Related Services Pronouncements* published by IFAC contains a complete listing of terms defined in the ISAs. It also includes descriptions of other terms found in ISAs to assist in common and consistent interpretation and translation.

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## **ISA 210, *Agreeing the Terms of Audit Engagements***

### **Introduction**

#### **Scope of this ISA**

1. This International Standard on Auditing (ISA) deals with the auditor’s responsibilities in agreeing the terms of the audit engagement with management and, where appropriate, those charged with governance. This includes establishing that certain preconditions for an audit, responsibility for which rests with management and, where appropriate, those charged with governance, are present. ISA 220 (Revised) deals with those aspects of engagement acceptance that are within the control of the auditor. (Ref: Para. A1)

...

#### **Application and Other Explanatory Material**

##### **Scope of this ISA (Ref: Para. 1)**

- A1. ~~ISQM 1 deals with the firm’s responsibilities regarding the acceptance and continuance of client relationships and specific engagements. Assurance engagements, which include audit engagements, may only be accepted when the practitioner considers that relevant ethical requirements such as independence and professional competence will be satisfied, and when the engagement exhibits certain characteristics.~~ The auditor’s responsibilities in respect of relevant ethical requirements, including those related to independence, in the context of the acceptance of an audit engagement and in so far as they are within the control of the auditor are dealt with in ISA 220 (Revised).<sup>26</sup> This ISA deals with those matters (or preconditions) that are within the control of the entity and upon which it is necessary for the auditor and the entity’s management to agree.

...

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<sup>26</sup> ISA 220 (Revised), paragraphs 9–11, 14–19



## ISA 230, *Audit Documentation*

### Introduction

...

#### Nature and Purposes of Audit Documentation

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3. Audit documentation serves a number of additional purposes, including the following:
- Assisting the engagement team to plan and perform the audit.
  - Assisting members of the engagement team responsible for supervision to direct and supervise the audit work, and to discharge their review responsibilities in accordance with ISA 220 (Revised).<sup>27</sup>
  - Enabling the engagement team to be accountable for its work.
  - Retaining a record of matters of continuing significance to future audits.
  - Enabling the conduct of engagement quality control reviews,<sup>28</sup> other engagement reviews and monitoring activities under the firm's system of quality management inspections in accordance with ISQC 1<sup>29</sup> ~~or national requirements that are at least as demanding.~~<sup>30</sup>
  - Enabling the conduct of external inspections in accordance with applicable legal, regulatory or other requirements.

...

#### Application and Other Explanatory Material

...

##### Documentation of the Audit Procedures Performed and Audit Evidence Obtained

...

*Form, Content and Extent of Audit Documentation* (Ref: Para. 8)

...

Documentation of Compliance with ISAs (Ref: Para. 8(a))

...

- A7. 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

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<sup>27</sup> ISA 220 (Revised), *Quality Control for an Audit of Financial Statements*, paragraphs 15–17, 27–31

<sup>28</sup> International Standard on Quality Management (ISQM) 2, *Engagement Quality Reviews*

<sup>29</sup> ISQC 1, *Quality Control for Firms that Perform Audits and Reviews of Financial Statements, and Other Assurance and Related Services Engagements*, paragraphs 32–33, 35–38, and 48

<sup>30</sup> ISA 220 (Revised), paragraph 2

a checklist, for example) compliance with matters for which compliance is demonstrated by documents included within the audit file. For example:

- The existence of an adequately documented audit plan demonstrates that the auditor has planned the audit.
- The existence of a signed engagement letter in the audit file demonstrates that the auditor has agreed the terms of the audit engagement with management or, where appropriate, those charged with governance.
- An auditor's report containing an appropriately qualified opinion on the financial statements demonstrates that the auditor has complied with the requirement to express a qualified opinion under the circumstances specified in the ISAs.
- In relation to requirements that apply generally throughout the audit, there may be a number of ways in which compliance with them may be demonstrated within the audit file:
  - For example, there may be no single way in which the auditor's professional skepticism is documented. But the audit documentation may nevertheless provide evidence of the auditor's exercise of professional skepticism in accordance with the ISAs. Such evidence may include specific procedures performed to corroborate management's responses to the auditor's inquiries.
  - Similarly, that the engagement partner has taken responsibility for the nature, timing and extent of direction, and supervision and performance of the audit in compliance with engagement team and the ISAs review of the work performed may be evidenced in a number of ways within the audit documentation. This may include documentation of that evidences the engagement partner's timely sufficient and appropriate involvement in aspects of the audit, such as participation in the engagement team discussions required by ISA 315 (Revised).<sup>34</sup>

...

*Identification of Specific Items or Matters Tested, and of the Preparer and Reviewer* (Ref: Para. 9)

...

A13. ISA 220 (Revised) contains requirements and guidance on the requires the auditor to review the audit work performed through review of the audit documentation.<sup>32</sup> The requirement to document who reviewed the audit work performed does not imply a need for each specific working paper to include evidence of review. The requirement, however, means documenting what audit work was reviewed, who reviewed such work, and when it was reviewed.

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<sup>34</sup> ISA 315, *Identifying and Assessing the Risks of Material Misstatement through Understanding the Entity and Its Environment*, paragraph 10

<sup>32</sup> ISA 220 (Revised), paragraphs 1728–29

*Matters Arising after the Date of the Auditor's Report* (Ref: Para. 13)

A20. Examples of exceptional circumstances include facts which become known to the auditor after the date of the auditor's report but which existed at that date and which, if known at that date, might have caused the financial statements to be amended or the auditor to modify the opinion in the auditor's report.<sup>33</sup> The resulting changes to the audit documentation are reviewed in accordance with the review responsibilities set out in ISA 220 (Revised).<sup>34</sup> ~~with the engagement partner taking final responsibility for the changes.~~

**Assembly of the Final Audit File** (Ref: Para. 14–16)

A21. ISQGM 1 (or national requirements that are at least as demanding) requires firms to establish policies ~~and/or procedures that require the engagement files to be assembled within an appropriate period of time after the engagement reports have been finalized for the timely completion of the assembly of audit files.~~<sup>35</sup> An appropriate time limit within which to complete the assembly of the final audit file is ordinarily not more than 60 days after the date of the auditor's report.<sup>36</sup>

...

A23. ISQGM 1 (or national requirements that are at least as demanding) requires firms to establish policies ~~and/or procedures for the retention of engagement documentation~~ that require the engagement documentation to be retained and maintained to meet the needs of the firm and to comply with law, regulation, relevant ethical requirements, or other professional standards.<sup>37</sup> The retention period for audit engagements ordinarily is no shorter than five years from the date of the auditor's report, or, if later, the date of the ~~group auditor's report on the group financial statements, when applicable.~~<sup>38</sup>

A24. An example of a circumstance in which the auditor may find it necessary to modify existing audit documentation or add new audit documentation after file assembly has been completed is the need to clarify existing audit documentation arising from comments received during monitoring ~~inspections performed by internal activities or external parties inspections.~~

## Appendix

(Ref: Para. 1)

### Specific Audit Documentation Requirements in Other ISAs

This appendix identifies paragraphs in other ISAs that contain specific documentation requirements. The list is not a substitute for considering the requirements and related application and other explanatory material in ISAs.

- ISA 210, *Agreeing the Terms of Audit Engagements* – paragraphs 10–12

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<sup>33</sup> ISA 560, *Subsequent Events*, paragraph 14

<sup>34</sup> ISA 220 (Revised), paragraph 4627

<sup>35</sup> ISQGM 1, paragraph 4537(f)(i)

<sup>36</sup> ISQGM 1, paragraph A54A110

<sup>37</sup> ISQGM 1, paragraph 4737(f)(ii)

<sup>38</sup> ISQGM 1, paragraph A64A111

- ISA 220 (Revised), *Quality Control Management for an Audit of Financial Statements* – paragraphs 24–25<sup>38</sup>

...

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

...

### **Application and Other Explanatory Material**

...

#### **Audit Procedures When Non-Compliance Is Identified or Suspected**

...

*Evaluating the Implications of Identified or Suspected Non-Compliance (Ref: Para. 22)*

...

A25. In certain circumstances, the auditor may consider withdrawing from the engagement, where permitted by law or regulation, for example when management or those charged with governance do not take the remedial action that the auditor considers appropriate in the circumstances or the identified or suspected non-compliance raises questions regarding the integrity of management or those charged with governance, even when the non-compliance is not material to the financial statements. The auditor may consider it appropriate to obtain legal advice to determine whether withdrawal from the engagement is appropriate. When the auditor determines that withdrawing from the engagement would be appropriate, doing so would not be a substitute for complying with other responsibilities under law, regulation or relevant ethical requirements to respond to identified or suspected non-compliance. Furthermore, paragraph A9A49 of ISA 220<sup>39</sup> (Revised) indicates that some ethical requirements may require the predecessor auditor, upon request by the proposed successor auditor, to provide information regarding non-compliance with laws and regulations to the successor auditor.

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

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### **Application and Other Explanatory Material**

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#### **Matters to Be Communicated**

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*Significant Findings from the Audit (Ref: Para. 16)*

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<sup>39</sup> ISA 220, *Quality Control for an Audit of Financial Statements*

...

Other Significant Matters Relevant to the Financial Reporting Process (Ref: Para. 16(e))

...

A28. To the extent not already addressed by the requirements in paragraphs 16(a)–(d) and related application material, the auditor may consider communicating about other matters discussed with, or considered by, the engagement quality control reviewer, if one has been appointed, ~~in accordance with ISA 220.~~<sup>40</sup>

...

## Appendix 1

### Specific Requirements in ISQCM 1 and Other ISAs that Refer to Communications with Those Charged With Governance

This appendix identifies paragraphs in ISQCM 1<sup>41</sup> and other ISAs that require communication of specific matters with those charged with governance. The list is not a substitute for considering the requirements and related application and other explanatory material in ISAs.

- ISQCM 1, *Quality Control/Management for Firms that Perform Audits and/or Reviews of Financial Statements, and/or Other Assurance and/or Related Services Engagements* – paragraph 30(a)41(c)

...

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## ISA 300, *Planning an Audit of Financial Statements*

### Introduction

#### Scope of this ISA

1. This International Standard on Auditing (ISA) deals with the auditor's responsibility to plan an audit of financial statements. This ISA is written in the context of recurring audits. Additional considerations in an initial audit engagement are separately identified.

#### The Role and Timing of Planning

2. Planning an audit involves establishing the overall audit strategy for the engagement and developing an audit plan. Adequate quality management at the engagement level in accordance with ISA 220 (Revised), in conjunction with adequate planning in accordance with this ISA, benefits the audit of financial statements in several ways, including the following: (Ref: Para. A1A0–A3)
  - Helping the auditor to devote appropriate attention to important areas of the audit.
  - Helping the auditor identify and resolve potential problems on a timely basis.

<sup>40</sup> See paragraphs 19–22 and A23–A33 of ISA 220, *Quality Control for an Audit of Financial Statements*.

<sup>41</sup> ISQCM 1, *Quality Control/Management for Firms that Perform Audits and/or Reviews of Financial Statements, and/or Other Assurance and/or Related Services Engagements*

- Helping the auditor properly organize and manage the audit engagement so that it is performed in an effective and efficient manner.
- Assisting in the selection of engagement team members with appropriate levels of capabilities and competence to respond to anticipated risks, and the proper assignment of work to them.
- Facilitating the direction and supervision of engagement team members and the review of their work.
- Assisting, where applicable, in coordination of work done by auditors of components and experts.

...

## Requirements

...

### Preliminary Engagement Activities

6. The auditor shall undertake the following activities at the beginning of the current audit engagement:
  - (a) Performing procedures required by ISA 220 (Revised) regarding the acceptance and continuance of the client relationship and the specific audit engagement,<sup>42</sup>
  - (b) Evaluating compliance with relevant ethical requirements, including those related to independence, in accordance with ISA 220 (Revised);<sup>43</sup> and
  - (c) Establishing an understanding of the terms of the engagement, as required by ISA 210.<sup>44</sup> (Ref: Para. A5–A7)

...

### Planning Activities

...

8. In establishing the overall audit strategy, the auditor shall consider the information obtained from complying with the requirements of ISA 220 (Revised) and:
  - (a) Identify the characteristics of the engagement that define its scope;
  - (b) Ascertain the reporting objectives of the engagement to plan the timing of the audit and the nature of the communications required;
  - (c) Consider the factors that, in the auditor's professional judgment, are significant in directing the engagement team's efforts;
  - (d) Consider the results of preliminary engagement activities and, where applicable, whether knowledge gained on other engagements performed by the engagement partner for the entity is relevant; and

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<sup>42</sup> ISA 220 (Revised), *Quality Control/Management for an Audit of Financial Statements*, paragraphs 42–43 and 20–22

<sup>43</sup> ISA 220 (Revised), paragraphs 9–11 and 14–19

<sup>44</sup> ISA 210, *Agreeing the Terms of Audit Engagements*, paragraphs 9–13

- (e) Ascertain the nature, timing and extent of resources necessary to perform the engagement. (Ref: Para. A8–A11)

...

- 11. The auditor shall plan the nature, timing and extent of direction and supervision of engagement team members and the review of their work as required by ISA 220 (Revised). (Ref: Para. A16–A17)

...

### **Additional Considerations in Initial Audit Engagements**

- 13. The auditor shall undertake the following activities prior to starting an initial audit:
  - (a) Performing procedures required by ISA 220 (Revised) regarding the acceptance of ~~the client relationships and the specific audit engagements;~~<sup>45</sup> and
  - (b) Communicating with the predecessor auditor, where there has been a change of auditors, in compliance with relevant ethical requirements. (Ref: Para. A22)

...

### **Application and Other Explanatory Material**

A0. ISA 220 (Revised) establishes requirements and provides guidance on the specific responsibilities of the auditor regarding quality management at the engagement level for an audit of financial statements, and the related responsibilities of the engagement partner. Information obtained from complying with the requirements of ISA 220 (Revised) is relevant to this ISA. For example, in accordance with ISA 220 (Revised), the engagement partner is required to determine that sufficient and appropriate resources to perform the engagement have been assigned or made available to the engagement team, given the nature and circumstances of the audit engagement. Such a determination is directly relevant when describing the nature, timing and extent of resources necessary to perform the engagement in the overall strategy, as required by paragraph 8 of this ISA.

### **The Role and Timing of Planning** (Ref: Para. 2)

A1. The nature and extent of planning activities will vary according to the size and complexity of the entity, the key engagement team members' previous experience with the entity, and changes in circumstances that occur during the audit engagement. In planning the audit, the auditor may use project management techniques and tools. ISA 220 (Revised)<sup>46</sup> describes how such techniques and tools may support the engagement partner and the other members of the engagement team in managing the quality of the engagement.

...

A3. The auditor may decide to discuss elements of planning with the entity's management to ~~facilitate the conduct and management of the audit engagement~~ inform quality management at the engagement level (for example, to coordinate some of the planned audit procedures with the work of the entity's personnel). Although these discussions often occur, the overall audit strategy and the audit plan

<sup>45</sup> ISA 220 (Revised), paragraphs ~~12–13~~20–22

<sup>46</sup> ISA 220 (Revised), paragraphs A63–A64

remain the auditor's responsibility. When discussing matters included in the overall audit strategy or audit plan, care is required in order not to compromise the effectiveness of the audit. For example, discussing the nature and timing of detailed audit procedures with management may compromise the effectiveness of the audit by making the audit procedures too predictable.

...

### **Preliminary Engagement Activities** (Ref: Para. 6)

- A5. Performing the preliminary engagement activities specified in paragraph 6 at the beginning of the current audit engagement assists the auditor in identifying and evaluating events or circumstances that may adversely affect the auditor's ability to ~~plan and perform the audit engagement~~manage quality at the engagement level in accordance with ISA 220 (Revised).
- A6. Performing ~~these~~ preliminary engagement activities enables the auditor to plan an audit engagement ~~for which~~in order to, for example:
- ~~The auditor maintains~~Maintain the necessary independence and ability to perform the engagement.
  - ~~There~~Determine that there are no issues with management integrity that may affect the auditor's willingness to continue the engagement.
  - ~~There~~Determine that there is no misunderstanding with the client as to the terms of the engagement.
- A7. ~~The auditor's consideration of client continuance and relevant ethical requirements, including independence, occurs throughout the audit engagement as conditions and changes in circumstances occur.~~ Performing initial procedures on both client continuance and evaluation of relevant ethical requirements (including independence) at the beginning of the current audit engagement means that they are completed prior to the performance of other significant activities for the current audit engagement. For continuing audit engagements, such initial procedures often occur shortly after (or in connection with) the completion of the previous audit.

### **Planning Activities**

#### *The Overall Audit Strategy* (Ref: Para. 7–8)

- A8. The process of establishing the overall audit strategy ~~assists the auditor to determine~~, subject to the completion of the auditor's risk assessment procedures, may include such matters as:
- The nature of resources (human, technological or intellectual) to be deployed for specific audit areas, ~~such as~~. For example, the use of deployment of appropriately experienced team members for high risk areas, or the involvement/assignment of experts to address complex matters;
  - The amount of resources to ~~allocate~~be allocated to specific audit areas, ~~such as~~. For example, the number of team members assigned to observe/attend the physical inventory count at material/multiple locations; the extent of review of other auditors' work in the case of group audits, or the audit budget in hours to allocate to high risk areas;
  - When these resources are to be deployed, such as whether at an interim audit stage or at key cutoff dates; and



- How such resources are ~~managed, directed and, supervised, such as~~ used. For example, when team briefing and debriefing meetings are expected to be held, how engagement partner and manager reviews are expected to take place (for example, on-site or off-site), ~~and whether to complete engagement quality reviews.~~

A8A. ISA 220 (Revised) contains requirements and guidance on engagement resources and engagement performance (including direction and supervision of the members of the engagement team and the review of the work performed).

...

#### *Direction, Supervision and Review (Ref: Para. 11)*

A16. ISA 220 (Revised)<sup>47</sup> establishes requirements and provides guidance on the engagement partner's responsibility for the nature, timing and extent of direction and supervision of the members of the engagement team and the review of the work performed. ~~The nature, timing and extent of the direction and supervision of engagement team members and review of their work vary depending on many factors, including:~~

- ~~The size and complexity of the entity.~~
- ~~The area of the audit.~~
- ~~The assessed risks of material misstatement (for example, an increase in the assessed risk of material misstatement for a given area of the audit ordinarily requires a corresponding increase in the extent and timeliness of direction and supervision of engagement team members, and a more detailed review of their work).~~
- ~~The capabilities and competence of the individual team members performing the audit work.~~

~~ISA 220 contains further guidance on the direction, supervision and review of audit work.<sup>48</sup>~~

#### *Considerations Specific to Smaller Entities*

A17. ~~If an audit is carried out entirely by the engagement partner, questions of direction and supervision of engagement team members and review of their work do not arise. In such cases, the engagement partner, having personally conducted all aspects of the work, will be aware of all material issues. Forming an objective view on the appropriateness of the judgments made in the course of the audit can present practical problems when the same individual also performs the entire audit. If particularly complex or unusual issues are involved, and the audit is performed by a sole practitioner, it may be desirable to consult with other suitably experienced auditors or the auditor's professional body.~~

#### **Documentation (Ref: Para. 12)**

A18. The documentation of the overall audit strategy is a record of the key decisions ~~considered necessary to properly plan the audit and~~ in managing quality at the engagement level and a means to communicate significant matters to the engagement team. For example, the auditor may summarize the overall audit strategy in the form of a memorandum that contains key decisions regarding the overall scope, timing and conduct of the audit.

<sup>47</sup> ISA 220 (Revised), paragraphs 27–29

<sup>48</sup> ISA 220, paragraphs 15–17

...

### **Additional Considerations in Initial Audit Engagements** (Ref: Para. 13)

A22. The purpose and objective of planning the audit are the same whether the audit is an initial or recurring engagement. However, for an initial audit, the auditor may need to expand the planning activities because the auditor does not ordinarily have the previous experience with the entity that is considered when planning recurring engagements. For an initial audit engagement, additional matters the auditor may consider in establishing the overall audit strategy and audit plan include the following:

- Unless prohibited by law or regulation, arrangements to be made with the predecessor auditor, for example, to review the predecessor auditor's working papers.
- Any major issues (including the application of accounting principles or of auditing and reporting standards) discussed with management in connection with the initial selection as auditor, the communication of these matters to those charged with governance and how these matters affect the overall audit strategy and audit plan.
- The audit procedures necessary to obtain sufficient appropriate audit evidence regarding opening balances.<sup>49</sup>
- ~~Other procedures required~~ responses designed and implemented by the firm's system of quality control ~~firm~~ for initial audit engagements (for example, e.g., the firm's system of quality control management may include responses that require the involvement of another partner or senior individual with appropriate authority to review the overall audit strategy prior to commencing significant audit procedures or to review reports prior to their issuance).

### **Appendix**

(Ref: Para. 7–8, A8–A11)

### **Considerations in Establishing the Overall Audit Strategy**

This appendix provides examples of matters the auditor may consider in ~~establishing the overall audit strategy~~ managing quality at the engagement level. Many of these matters will ~~also~~ influence the auditor's overall audit strategy and detailed audit plan. The examples provided cover a broad range of matters applicable to many engagements. While some of the matters referred to below may be required by other ISAs, not all matters are relevant to every audit engagement and the list is not necessarily complete.

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#### **Nature, Timing and Extent of Resources**

- The ~~selection~~ human, technological and intellectual resources assigned or made available to the engagement (e.g., assignment of the engagement team (including, where necessary, the engagement quality control reviewer) and the assignment of audit work to the team members, including the assignment of appropriately experienced team members to areas where there may be higher risks of material misstatement).

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<sup>49</sup> ISA 510, *Initial Audit Engagements—Opening Balances*

- Engagement budgeting, including considering the appropriate amount of time to set aside for areas where there may be higher risks of material misstatement.

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## ISA 500, *Audit Evidence*

...

### Application and Other Explanatory Material

#### Sufficient Appropriate Audit Evidence (Ref: Para. 6)

- A1. Audit evidence is necessary to support the auditor's opinion and report. It is cumulative in nature and is primarily obtained from audit procedures performed during the course of the audit. It may, however, also include information obtained from other sources such as previous audits (provided the auditor has determined whether changes have occurred since the previous audit that may affect its relevance to the current audit<sup>50</sup>) or ~~a firm's quality control procedures for client acceptance and continuance~~through the information obtained by the firm in the acceptance or continuance of the client relationship or engagement. In addition to other sources inside and outside the entity, the entity's accounting records are an important source of audit evidence. Also, information that may be used as audit evidence may have been prepared using the work of a management's expert. Audit evidence comprises both information that supports and corroborates management's assertions, and any information that contradicts such assertions. In addition, in some cases the absence of information (for example, management's refusal to provide a requested representation) is used by the auditor, and therefore, also constitutes audit evidence.

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#### Information to Be Used as Audit Evidence

##### *Relevance and Reliability* (Ref: Para. 7)

- A26. As noted in paragraph A1, while audit evidence is primarily obtained from audit procedures performed during the course of the audit, it may also include information obtained from other sources ~~such as, for example, previous audits, in certain circumstances, a firm's quality control procedures for client acceptance and continuance and~~through the information obtained by the firm in the acceptance or continuance of the client relationship or engagement and in complying with certain additional responsibilities under law, regulation or relevant ethical requirements (e.g., regarding an entity's non-compliance with laws and regulations). The quality of all audit evidence is affected by the relevance and reliability of the information upon which it is based.

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<sup>50</sup> ISA 315 (Revised), paragraph 9

## **ISA 540 (Revised), Auditing Accounting Estimates and Related Disclosures**

...

### **Application and Other Explanatory Material**

...

#### **Risk Assessment Procedures and Related Activities**

...

*Specialized Skills or Knowledge* (Ref: Para. 15)

A61. Matters that may affect the auditor's determination of whether the engagement team requires specialized skills or knowledge, include, for example:<sup>51</sup>

- The nature of the accounting estimates for a particular business or industry (for example, mineral deposits, agricultural assets, complex financial instruments, insurance contract liabilities).

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

### **Introduction**

#### **Scope of this ISA**

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4. In accordance with ISA 220 (Revised),<sup>52</sup> the group engagement partner is required to be satisfied that those performing the group audit engagement, including component auditors, collectively have the appropriate competence and capabilities, including sufficient time. The group engagement partner is also responsible for the direction, supervision and performance of the group audit engagement.
5. The group engagement partner applies the requirements of ISA 220 (Revised) regardless of whether the group engagement team or a component auditor performs the work on the financial information of a component. This ISA assists the group engagement partner to meet the requirements of ISA 220 (Revised) where component auditors perform work on the financial information of components.

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<sup>51</sup> ISA 220 (Revised), *Quality Control/Management for an Audit of Financial Statements*, paragraphs 1423–24 and ISA 300, *Planning an Audit of Financial Statements*, paragraph 8(e)

<sup>52</sup> ISA 220 (Revised), *Quality Control/Management for an Audit of Financial Statements*, paragraphs 14–15

## Requirements

...

### Acceptance and Continuance

12. In applying ISA 220 (Revised), the group engagement partner shall determine whether sufficient appropriate audit evidence can reasonably be expected to be obtained in relation to the consolidation process and the financial information of the components on which to base the group audit opinion. For this purpose, the group engagement team shall obtain an understanding of the group, its components, and their environments that is sufficient to identify components that are likely to be significant components. Where component auditors will perform work on the financial information of such components, the group engagement partner shall evaluate whether the group engagement team will be able to be involved in the work of those component auditors to the extent necessary to obtain sufficient appropriate audit evidence. (Ref: Para. A10–A12)

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## ISA 610 (Revised 2013), *Using the Work of Internal Auditors*

### Introduction

...

### Requirements

...

#### Using Internal Auditors to Provide Direct Assistance

...

34. The external auditor shall direct, supervise and review the work performed by internal auditors on the engagement in accordance with ISA 220 (Revised).<sup>53</sup> In so doing:
- (a) The nature, timing and extent of direction, supervision, and review shall recognize that the internal auditors are not independent of the entity and be responsive to the outcome of the evaluation of the factors in paragraph 29 of this ISA; and
  - (b) The review procedures shall include the external auditor checking back to the underlying audit evidence for some of the work performed by the internal auditors.

The direction, supervision and review by the external auditor of the work performed by the internal auditors shall be sufficient in order for the external auditor to be satisfied that the internal auditors have obtained sufficient appropriate audit evidence to support the conclusions based on that work. (Ref: Para. A40–A41)

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<sup>53</sup> ISA 220 (Revised), *Quality Control/Management for an Audit of Financial Statements*

## Application and Other Explanatory Material

...

### Determining Whether, in Which Areas, and to What Extent the Work of the Internal Audit Function Can Be Used

#### *Evaluating the Internal Audit Function*

...

Application of a Systematic and Disciplined Approach (Ref: Para. 15(c))

...

A11. Factors that may affect the external auditor's determination of whether the internal audit function applies a systematic and disciplined approach include the following:

- The existence, adequacy and use of documented internal audit procedures or guidance covering such areas as risk assessments, work programs, documentation and reporting, the nature and extent of which is commensurate with the size and circumstances of an entity.
- Whether the internal audit function has appropriate quality control policies and procedures, for example, ~~such as those policies and procedures in ISQC 1<sup>54</sup>~~ that would be applicable to an internal audit function (such as those relating to leadership, human resources and engagement performance) or quality control requirements in standards set by the relevant professional bodies for internal auditors. Such bodies may also establish other appropriate requirements such as conducting periodic external quality assessments.

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## ISA 620, *Using the Work of an Auditor's Expert*

### Introduction

#### Scope of this ISA

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2. ISA does not deal with:
  - (a) Situations where the engagement team includes a member, or consults an individual or organization, with expertise in a specialized area of accounting or auditing, which are dealt with in ISA 220 (Revised);<sup>55</sup> or
  - (b) The auditor's use of the work of an individual or organization possessing expertise in a field other than accounting or auditing, whose work in that field is used by the entity to assist the

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<sup>54</sup> International Standard on Quality Control (ISQC) 1, *Quality Control for Firms that Perform Audits and Reviews of Financial Statements, and Other Assurance and Related Services Engagements*

<sup>55</sup> ISA 220 (Revised), *Quality Control/Management for an Audit of Financial Statements*, paragraphs A11, A21–A23A56

entity in preparing the financial statements (a management's expert), which is dealt with in ISA 500.<sup>56</sup>

...

## Requirements

...

### Nature, Timing and Extent of Audit Procedures

8. The nature, timing and extent of the auditor's procedures with respect to the requirements in paragraphs 9–13 of this ISA will vary depending on the circumstances. In determining the nature, timing and extent of those procedures, the auditor shall consider matters including: (Ref: Para. A10)
- (a) The nature of the matter to which that expert's work relates;
  - (b) The risks of material misstatement in the matter to which that expert's work relates;
  - (c) The significance of that expert's work in the context of the audit;
  - (d) The auditor's knowledge of and experience with previous work performed by that expert; and
  - (e) Whether that expert is subject to the auditor's firm's system of quality control policies and procedures management. (Ref: Para. A11–A13)

## Application and Other Explanatory Material

...

### Determining the Need for an Auditor's Expert (Ref: Para. 7)

...

- A6. If the preparation of the financial statements involves the use of expertise in a field other than accounting, the auditor, who is skilled in accounting and auditing, may not possess the necessary expertise to audit those financial statements. The engagement partner is required to be satisfied that the engagement team, and any auditor's experts who are not part of the engagement team, collectively have the appropriate competence and capabilities, including sufficient time, to perform the audit engagement.<sup>57</sup> Further, the auditor is required to ascertain the nature, timing and extent of resources necessary to perform the engagement.<sup>58</sup> The auditor's determination of whether to use the work of an auditor's expert, and if so when and to what extent, assists the auditor in meeting these requirements. As the audit progresses, or as circumstances change, the auditor may need to revise earlier decisions about using the work of an auditor's expert.

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<sup>56</sup> ISA 500, *Audit Evidence*, paragraphs A35–A49

<sup>57</sup> ISA 220 (Revised), paragraph 1424

<sup>58</sup> ISA 300, *Planning an Audit of Financial Statements*, paragraph 8(e)

**Nature, Timing and Extent of Audit Procedures** (Ref: Para. 8)

A10. The nature, timing and extent of audit procedures with respect to the requirements in paragraphs 9–13 of this ISA will vary depending on the circumstances. For example, the following factors may suggest the need for different or more extensive procedures than would otherwise be the case:

- The work of the auditor's expert relates to a significant matter that involves subjective and complex judgments.
- The auditor has not previously used the work of the auditor's expert, and has no prior knowledge of that expert's competence, capabilities and objectivity.
- The auditor's expert is performing procedures that are integral to the audit, rather than being consulted to provide advice on an individual matter.
- The expert is an auditor's external expert and is not, therefore, subject to the firm's system of quality control policies and procedures management.

*The Auditor's Firm's System of Quality Control Policies and Procedures Management* (Ref: Para. 8(e))

A11. An auditor's internal expert may be a partner or staff, including temporary staff, of the auditor's firm, and therefore subject to the system of quality control policies and procedures management of that firm in accordance with ISQGM 1<sup>59</sup> or national requirements that are at least as demanding.<sup>60</sup> ~~Alternatively, an~~ An auditor's internal expert may also be a partner or staff, including temporary staff, of a network firm, which may share common quality control management policies and/or procedures with the auditor's firm.

A12. An auditor's external expert is not a member of the engagement team and is not subject to ~~quality control policies and procedures in accordance with ISQC 1.~~<sup>64</sup> ~~In some jurisdictions, however, the~~ firm's system of quality management in accordance with ISQM 1.<sup>62</sup> However, ISQM 1 includes requirements for the firm when the firm intends to obtain or use resources provided by a service provider in performing engagements, which includes the use of an external expert.<sup>63</sup> Relevant ethical requirements or law or regulation may require that an auditor's external expert be treated as a member of the engagement team, and the external expert may therefore be subject to relevant ethical requirements, including those pertaining related to independence, and other professional requirements, as determined by ~~that~~ the relevant ethical requirements or law or regulation.

A13. ~~Engagement teams are entitled to rely on the firm's system of quality control, unless information provided by the firm or other parties suggests otherwise.~~<sup>64</sup> ~~The extent of that reliance will vary with the circumstances, and may affect the nature, timing and extent of the auditor's procedures with respect to such matters as~~ As described in ISA 220 (Revised),<sup>65</sup> quality management at the

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<sup>59</sup> ISQGM 1, Quality Control Management for Firms that Perform Audits and/or Reviews of Financial Statements, and/or Other Assurance and/or Related Services Engagements, paragraph 1219(f)

<sup>60</sup> ISA 220 (Revised), paragraph 23

<sup>64</sup> ISQC 1, paragraph 12(f)

<sup>62</sup> ISQM 1, paragraph 19(f)

<sup>63</sup> ISQM 1, paragraphs 64–65

<sup>64</sup> ISA 220, paragraph 4

<sup>65</sup> ISA 220 (Revised), paragraph A5



engagement level is supported by the firm's system of quality management and informed by the specific nature and circumstances of the audit engagement. The auditor may be able to depend on the firm's related policies or procedures in respect of:

- Competence and capabilities, through recruitment and training programs.
- Objectivity. Auditor's internal experts are subject to relevant ethical requirements, including those ~~pertaining~~relating to independence.
- The auditor's evaluation of the adequacy of the auditor's expert's work. For example, the firm's training programs may provide auditor's internal experts with an appropriate understanding of the interrelationship of their expertise with the audit process. Reliance on such training and other firm ~~processes, such as protocols for scoping the work of auditor's internal experts,~~ may affect the nature, timing and extent of the auditor's procedures to evaluate the adequacy of the auditor's expert's work.
- Adherence to regulatory and legal requirements, through monitoring processes.
- Agreement with the auditor's expert.

~~Such reliance~~Matters that the auditor may take into account when determining whether, and if so, the degree to which, the auditor may depend on the firm's policies or procedures are described in ISA 220 (Revised). Dependence on the firm's policies or procedures does not reduce the auditor's responsibility to meet the requirements of this ISA.

#### **The Competence, Capabilities and Objectivity of the Auditor's Expert (Ref: Para. 9)**

...

- A15. Information regarding the competence, capabilities and objectivity of an auditor's expert may come from a variety of sources, such as:
- Personal experience with previous work of that expert.
  - Discussions with that expert.
  - Discussions with other auditors or others who are familiar with that expert's work.
  - Knowledge of that expert's qualifications, membership of a professional body or industry association, license to practice, or other forms of external recognition.
  - Published papers or books written by that expert.
  - The auditor's firm's system of quality control policies and procedures~~management~~ (see paragraphs A11–A13).
- A18. A broad range of circumstances may threaten objectivity, for example, self-interest threats, advocacy threats, familiarity threats, self-review threats, and intimidation threats. Safeguards may eliminate or reduce such threats, and may be created by external structures (~~for example, e.g.,~~ the auditor's expert's profession, legislation or regulation), or by the auditor's expert's work environment (~~for example, quality control, e.g.,~~ the firm's policies and/or procedures or the external expert's organization's policies or procedures). There may also be safeguards specific to the audit engagement.

...

**Agreement with the Auditor's Expert** (Ref: Para. 11)

...

A26. When there is no written agreement between the auditor and the auditor's expert, evidence of the agreement may be included in, for example:

- Planning memoranda, or related working papers such as the audit program.
- The policies ~~and~~ procedures of the auditor's firm's system of quality management. In the case of an auditor's internal expert, the ~~established policies and procedures~~requirements to which that expert is subject under the firm's system of quality management may include, for example, particular policies ~~and~~ procedures in relation to that expert's work. The extent of documentation in the auditor's working papers depends on the nature of such policies ~~and~~ procedures. For example, no documentation may be required in the auditor's working papers if the auditor's firm has detailed protocols covering the circumstances in which the work of such an expert is used.

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

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**Application and Other Explanatory Material**

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**Auditor's Report** (Ref: Para. 20)

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*Auditor's Report for Audits Conducted in Accordance with International Standards on Auditing*

...

Name of the Engagement Partner (Ref: Para. 46)

A61. ~~ISQC 1<sup>66</sup> requires that~~ The objective of the firm establish policies in ISQM 1<sup>67</sup> is to design, implement and procedures to provide operate a system of quality management that provides the firm with reasonable assurance that engagements are performed;

- 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

<sup>66</sup> ISQC 1, *Quality Control for Firms that Perform Audits and Reviews of Financial Statements, and Other Assurance and Related Services Engagements*, paragraph 32

<sup>67</sup> ISQM 1, *Quality Control for Firms that Perform Audits or Reviews of Financial Statements, or Other Assurance or Related Services Engagements*, paragraph 18

- Engagement reports issued by the firm or engagement partners are appropriate in the circumstances.

Notwithstanding ~~these~~ the objective of ISQCM 1 requirements, naming the engagement partner in the auditor's report is intended to provide further transparency to the users of the auditor's report on financial statements of a listed entity.

...

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

...

### **Application and Other Explanatory Material**

...

#### **Determining Key Audit Matters** (Ref: Para. 9–10)

...

#### *Matters that Required Significant Auditor Attention* (Ref: Para. 9)

...

A15. Various ISAs require specific communications with those charged with governance and others that may relate to areas of significant auditor attention. For example:

- ISA 260 (Revised) requires the auditor to communicate significant difficulties, if any, encountered during the audit with those charged with governance.<sup>68</sup> The ISAs acknowledge potential difficulties in relation to, for example:
  - Related party transactions,<sup>69</sup> in particular limitations on the auditor's ability to obtain audit evidence that all other aspects of a related party transaction (other than price) are equivalent to those of a similar arm's length transaction.
  - Limitations on the group audit, for example, where the group engagement team's access to information may have been restricted.<sup>70</sup>
- ISA 220 (Revised) establishes requirements for the engagement partner in relation to undertaking appropriate consultation on matters where the firm's policies or procedures require consultation, difficult or contentious matters,<sup>71</sup> and other matters that in the engagement

<sup>68</sup> ISA 260 (Revised), paragraphs 16(b) and A21

<sup>69</sup> ISA 550, *Related Parties*, paragraph A42

<sup>70</sup> ISA 600, *Special Considerations—Audits of Group Financial Statements (Including the Work of Component Auditors)*, paragraph 49(d)

<sup>71</sup> ISA 220 (Revised), *Quality Control/Management for an Audit of Financial Statements*, paragraph 48~~32~~

partner's professional judgment, require consultation. For example, the auditor may have consulted with others within the firm or outside the firm on a significant technical matter, which may be an indicator that it is a key audit matter. The engagement partner is also required to discuss, among other things, significant matters arising during the audit engagement with the engagement quality ~~control~~ reviewer.<sup>72</sup>

...

#### **Communication with Those Charged with Governance** (Ref: Para. 17)

...

A63. The requirement in paragraph 17(b) to communicate with those charged with governance when the auditor has determined there are no key audit matters to communicate in the auditor's report may provide an opportunity for the auditor to have further discussion with others who are familiar with the audit and the significant matters that may have arisen (including the engagement quality ~~control~~ reviewer, where one has been appointed). These discussions may cause the auditor to re-evaluate the auditor's determination that there are no key audit matters.

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### **ISA 720 (Revised), *The Auditor's Responsibilities Relating to Other Information***

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#### **Application and Other Explanatory Material**

...

#### **Reading and Considering the Other Information** (Ref: Para. 14–15)

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A24. In accordance with ISA 220 (Revised),<sup>73</sup> the engagement partner is required to take responsibility for the direction, supervision and performance of the audit engagement, nature, timing and extent of direction and supervision of the members of the engagement team and the review of the work performed, and be satisfied that such direction, supervision and review is in compliance with the firm's policies or procedures, professional standards and applicable legal and regulatory requirements. In the context of this ISA, factors that may be taken into account when determining the appropriate engagement team members to address the requirements of paragraphs 14–15, include:

- The relative experience of engagement team members.
- Whether the engagement team members to be assigned the tasks have the relevant knowledge obtained in the audit to identify inconsistencies between the other information and that knowledge.

<sup>72</sup> ISA 220 (Revised), paragraph 19.33

<sup>73</sup> ISA 220 (Revised), *Quality Control/Management for an Audit of Financial Statements*, paragraph 15.27(a)

- The degree of judgment involved in addressing the requirements of paragraph 14–15. For example, performing procedures to evaluate the consistency of amounts in the other information that are intended to be the same as amounts in the financial statements may be carried out by less experienced engagement team members.
- Whether, in the case of a group audit, it is necessary to make inquiries of a component auditor in addressing the other information related to that component.

...

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## **IAPN 1000, *Special Considerations in Auditing Financial Instruments***

### **Contents**

International Auditing Practice Note (IAPN) 1000, *Special Considerations in Auditing Financial Instruments*, should be read in conjunction with the *Preface to the International Quality ~~Control~~Management, Auditing, Review, Other Assurance, and Related Services Pronouncements*. IAPNs do not impose additional requirements on auditors beyond those included in the International Standards on Auditing (ISAs), nor do they change the auditor's responsibility to comply with all ISAs relevant to the audit. IAPNs provide practical assistance to auditors. They are intended to be disseminated by those responsible for national standards, or used in developing corresponding national material. They also provide material that firms can use in developing their training programs and internal guidance.

...

## **Section II—Audit Considerations Relating to Financial Instruments**

...

Planning Considerations<sup>74</sup>

...

*Using Those with Specialized Skills and Knowledge in the Audit*<sup>75</sup>

<sup>74</sup> ISA 300, *Planning an Audit of Financial Statements*, deals with the auditor's responsibility to plan an audit of financial statements.

<sup>75</sup> When such a person's expertise is in auditing and accounting, regardless of whether the person is from within or external to the firm, this person is considered to be part of the engagement team and is subject to the requirements of ISA 220 *(Revised)*, *Quality ~~Control~~Management for an Audit of Financial Statements*. When such a person's expertise is in a field other than accounting or auditing, such person is considered to be an auditor's expert, and the provisions of ISA 620, *Using the Work of an Auditor's Expert*, apply. ISA 620 explains that distinguishing between specialized areas of accounting or auditing, and expertise in another field, will be a matter of professional judgment, but notes the distinction may be made between expertise in methods of accounting for financial instruments (accounting and auditing expertise) and expertise in complex valuation techniques for financial instruments (expertise in a field other than accounting or auditing).

78. A key consideration in audits involving financial instruments, particularly complex financial instruments, is the competence of the auditor. ISA 220 (Revised)<sup>76</sup> requires the engagement partner to be satisfied that members of the engagement team, and any auditor's experts who are not part of the engagement team, collectively have the ~~appropriate~~ competence and capabilities, including sufficient time, to perform the audit engagement ~~in accordance with professional standards and applicable legal and regulatory requirements and to enable an auditor's report that is appropriate in the circumstances to be issued.~~ Further, relevant ethical requirements<sup>77</sup> require the auditor to determine whether acceptance of the engagement would create any threats to compliance with the fundamental principles, including the professional competence and due care. Paragraph 79 below provides examples of the types of matters that may be relevant to the auditor's considerations in the context of financial instruments.

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<sup>76</sup> ISA 220 (Revised), paragraph 1424

<sup>77</sup> IESBA *Code of Ethics for Professional Accountants* paragraphs 210.1 and 210.6

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