Risk Management

Module 7

CONTENTS

7.1 Introduction

The concept of risk is not new to practitioners. It has been around as long as the profession has provided services in a commercial setting. However, the issue of risk and risk management has increased in importance as the number and size of legal claims has increased over the years.

You will notice this module is entitled risk management, not risk elimination. This is an important distinction and key to the material covered—mostly it is about managing the risks you can identify and, if possible, eliminating them. However, even if you can't completely eliminate most of the risks associated with being a practitioner, you can reduce and manage them to an acceptable level.

Risk management has a specific impact on life in an accounting firm. It is important in terms of protecting the assets, finances and operations of the firm and contributing to satisfactory legal compliance, corporate governance and due diligence. Consequently, risk management will protect the reputation, credibility and status of the firm.

Establish a risk management "culture" in the firm. A risk management culture emphasizes at all levels of your firm the importance of managing risk as part of each staff member's daily activities at all levels of the firm. The goal of creating a risk management culture is to create a situation where partners and staff instinctively look for risks and consider their impacts when making effective operational decisions. The essence of a risk management culture is that it is not geographically dependent, or specific to any country or location. The principles in establishing this culture are universal and relevant to each locality.

The sections of this module cover the component parts of establishing a risk management culture. This module discusses ethical issues and their impact on the risk exposure of your firm. The client engagement process is examined, as well as how best to manage your risk in this area.

The module discusses quality control processes within an accounting firm, emphasizing the important role they play in assisting practitioners manage their risk in the day-to-day working of the firm. Business continuity planning and the key elements of prevention, preparedness, response and recovery are also covered. This also includes strategies to deal with the death, or incapacity of the practitioner.

The module concludes with a discussion on liability and insurance within your firm and reviews the types of insurance that are most relevant to it.

7.2 Professionalism and Ethics within the Firm

This section provides background and information regarding ethical issues for small to medium-sized firms. It discusses the nature and impact of different types of ethical issues in providing assurance and non-assurance services. A greater understanding of these issues will allow practitioners to be better equipped when they have to face these types of issues.

7.2.1 The Code of Ethics for Professional Accountants

The *International Code of Ethics for Professional Accountants (including International Independence Standards)* issued by the International Ethics Standards Board for Accountants (the IESBA Code) was developed for professional accountants internationally. To date, the Code has been adopted or is used as a basis for national ethics standards or the ethical codes of professional accountancy organizations in over 120 jurisdictions around the world, including 16 among the G-20. In addition, the 31 largest networks of firms around the world that comprise the Forum of Firms have aligned their policies and methodologies to conform to the Code for transnational audits. It is reviewed and updated by IESBA from time-to-time, as appropriate. The IESBA Code was significantly revised and restructured with an effective date of June 15, 2019.

This module has used the revised and restructured IESBA Code as a guide on how practitioners should deal with the ethical issues they face in small- and medium-sized practices (SMPs) and recommends that practitioners use it as a key resource.

The foundation of the IESBA Code is a principles-based conceptual framework. This was explicitly intended to be broadly applicable around the world. Such an approach allows for differences in legal systems and jurisdictional variations. The focus, therefore, is on underlying principles rather than on prescriptive regulations, as this allows professionals to apply the principles to their own circumstances. The IESBA Code essentially covers three key areas.

Firstly, it establishes the fundamental principles for professionalism and ethical behavior within the firm. Secondly, it identifies ethical risks and assists in evaluating the significance of these threats. Thirdly, it provides guidance on how to address those threats when they are not at an acceptable level including the possibility of applying suitable safeguards to eliminate or reduce the threats to an acceptable level.

A discussion of the five fundamental principles on which the IESBA Code is based appears below.

7.2.2 Fundamental Principles of the IESBA Code

Principle 1: Integrity

Act with integrity. Be straightforward and honest in all professional and business relationships. Integrity implies fair dealing and truthfulness. Disassociate from matters such as reports, returns or communications that are materially false or misleading, or that obscure or omit information that renders them misleading.

It is appropriate that integrity is listed as the first principle because it is the foundation on which professional behavior is built. It should also be the foundation stone on which your firm is built. Integrity should pervade all areas of your firm. It would be a worthwhile exercise to consider your organization chart and ensure that integrity is exercised in all key areas of operation. For instance, consider the key areas of marketing, operations, human resources and finance within your firm. You need to be sure each area operates with integrity.

Principle 2: Objectivity

Be objective. Do not compromise your professional or business judgment due to personal interest, bias, pressure or the interests of others. Your objectivity may be impaired if you perform a professional service where there is a relationship bias, which results in your judgment being compromised. Objectivity means not being influenced by outside interests; the practitioner makes up his or her own mind.

Principle 3: Professional competence and due care

Ensure all work is performed with professional competence and due care. Both you and your staff should possess the knowledge and relevant skill to ensure competent professional service.

This also means your firm must exercise reasonable care and diligence in applying technical and professional standards. Professional competence means having attained certain skills and knowledge and having the capability to perform the task. You should ensure competence is maintained through continuing professional development.

When undertaking an engagement, ensure that you and your staff act responsibly in accordance with the requirements of the assignment. You and your staff should be careful, thorough, and on time. Proper training and supervision must be given on an ongoing basis to ensure that all services are provided competently and with due care.

Principle 4: Confidentiality

Keep all client and firm information confidential. Do not disclose any client information outside the firm without authority, and do not use client information for personal gain or purpose. Be cautious at all times, including in a social environment, to ensure that information is kept confidential.

There are limited exceptions to the principle of confidentiality. You have a duty to disclose if authorized by the client and are required by law to do so. There may also be a duty to disclose when required to comply with quality review checks, or in response to an inquiry. Disclosure may also be made to protect the professional interests of an accountant in legal proceedings, or to comply with technical and ethical standards. This includes, in particular understanding and complying with the provisions of Section 360 of the IESBA Code dealing with "Responding to Non-Compliance with Laws and Regulations".

Principle 5: Professional behavior

A distinguishing mark of the accountancy profession is its acceptance of the responsibility to act in the public interest. This means that professional behavior requires a practitioner to put the interests of the clients and the public ahead of his or her own.

It also means complying with all relevant laws and regulations, and avoiding any action that may discredit the profession. This also applies when you promote or market professional services. Promotions must be made honestly and truthfully and not contain exaggerated claims, or disparaging references to the work of others.

There is no one definition of professional behavior, as it can be quite subjective and can vary from country to country. It is up to each professional to monitor and assess his or her own behavior and avoid any action that may discredit the profession.

Professional behavior applies internally and externally. The practitioner must ensure it applies to everyone within his or her own firm. This can apply to a broad range of areas but essentially applies to the very heart of the firm. For a firm to be a professional entity, it must exhibit professional behavior.

It also applies externally for the firm, in how the firm deals with all external parties. In all of these dealings, the firm itself must display professional behavior and act in a professional manner.

7.2.3 The Conceptual Framework

The circumstances in which professional accountants operate might create threats to compliance with the fundamental principles. It is important that all practitioners comply with the conceptual framework and the fundamental principles. The conceptual framework applies equally for auditors who, when applying the ISAs, must comply with specific independence standards when performing audit or assurance engagements.

The conceptual framework uses a threats and safeguards approach. It forms a separate section in the IESBA Code with provisions that describe a simple, three-staged process for considering whether or not circumstances or a situation creates threats to compliance with the fundamental principles, and if so, whether such threats are at an acceptable level and what should be done as a result. The stages of the conceptual framework involve identifying, evaluating and addressing those threats by eliminating them or reducing them to an acceptable level.

A description of the conceptual framework is set out in Section 120 of the IESBA Code.

The provisions of Section 120 are not intended to be a "step-by-step" checklist. Rather they specify a logical and systematic approach for practitioners to identify, evaluate and address threats irrespective of the facts and circumstances. The provisions in the subsequent sections of the Code build on the provisions of the conceptual framework, and provide general and context-specific guidance depending on the specific facts and circumstances of a particular service, including outright prohibitions in certain cases. Therefore, those subsequent sections are incremental in nature and do not repeat the material included in Section 120.

When applying the conceptual framework, the practitioner has an overarching requirement to:

a) Exercise professional judgment;

b) Remain alert for new information and changes in facts and circumstances; and

c) Use the reasonable and informed third party test.

Exercise of Professional Judgment

Professional judgment involves the application of relevant training, professional knowledge, skill and experience commensurate with the facts and circumstances, including the nature and scope of the particular professional activities, and the interests and relationships involved. The exercise of professional judgment is required when the practitioner applies the conceptual framework in order to make informed decisions about the courses of actions available, and to determine whether such decisions are appropriate in the circumstances.

An understanding of known facts and circumstances is essential to the proper application of the conceptual framework. Determining the actions necessary to obtain this understanding and coming to a conclusion about whether the fundamental principles have been complied with all require the exercise of professional judgment.

In exercising professional judgment to obtain this understanding, the practitioner might consider whether:

- There is reason to be concerned that potentially relevant information might be missing from the facts and circumstances known to the practitioner.
- There is an inconsistency between the known facts and circumstances and the practitioner's expectations.
- The practitioner's experience and expertise are sufficient to reach a conclusion.
- There is a need to consult with others with relevant experience and expertise.
- The information provides a reasonable basis on which to reach a conclusion.
- The practitioner's own preconception or bias might be affecting the practitioner's exercise of professional judgment.
- There might be other reasonable conclusions to reach based on the available information.

Reasonable and Informed Third Party

As noted, the practitioner will use the reasonable and informed third party test when applying the conceptual framework. The reasonable and informed third party test is a consideration by the practitioner about whether the same conclusions would be reached by another party. This consideration is made from the perspective of a reasonable and informed third party, who weighs all of the relevant facts and circumstances that the accountant knows, or could reasonably expected to know, at the time the conclusions are made.

7.2.3a Identifying Threats

The conceptual framework requires the practitioner to identify threats to compliance with the fundamental principles. This includes identifying threats to independence when applicable. An understanding of the facts and circumstances, including any professional activities, interests and relationships, that might compromise compliance with the fundamental principles, is essential to the practitioner's identification of such compliance.

The existence of certain conditions, policies and procedures established by the profession, legislation, regulation, the firm or the client that can help the practitioner acting ethically might also help identify threats to compliance with the fundamental principles.

Examples of such conditions, policies and procedures include:

- • Corporate governance requirements.
- • Educational, training and experience requirements for the profession.
- • Effective complaint systems which enable the practitioner and the general public to draw attention to unethical behavior.
- • An explicit stated duty to report breaches of ethics requirements.
- • Professional or regulatory monitoring and disciplinary procedures.

Threats to compliance with the fundamental principles might be created by a broad range of facts and circumstances. It is not possible to define every situation that create threats. In addition, the nature of engagements and work assignments might differ and, consequently different types of threats might be created.

It is important to note that threats to complying with the independence standards are the same as the threats to comply with the fundamental principles. Threats to compliance with the fundamental principles and independence fall into one or more of five categories. These are discussed below with examples given for each.

1. Self-interest

The threat is that you will act in your self-interest over the interest of your client. A financial or other interest may inappropriately influence your judgment or behavior.

2. Self-review

The threat that you will not appropriately evaluate the results of a previous judgment made or activity performed, whether by you or by another individual within your firm on which you will rely in forming a judgement as part of performing a current activity. This arises when you have to evaluate or form a judgment on a past service provided by your firm, or by yourself.

3. Advocacy

The threat arises when you advocate the position or interest of your client or the firm by which you are employed. You may promote a particular position in favor of certain interests to the point that your objectivity is compromised.

4. Familiarity

The threat arises when you become too familiar with your client. A long or close relationship with a client, or a related party may mean you may become too sympathetic toward their interests or too accepting of their work.

5. Intimidation

The threat arises when you are intimidated e.g., by your client to act in a certain way. You may be placed under pressure or undue influence to act in a certain way, and your objectivity may become compromised. The pressures may be actual, or perceived.

Each of these ethics threats could occur on its own at some stage during the client relationship. A circumstance may create more than one threat, and a threat might affect compliance with more than one fundamental principle. In extreme cases, all five ethics threats could occur together. This may place the practitioner and their firm under extreme pressure to compromise their fundamental principles and ethical position.

Examples of ethics threats

The IESBA Code also provides some examples of ethics threats to use as a guide—however, it is impossible for all threats to be identified or described. The overriding principle is that professional accountants should not knowingly engage in any business, occupation or relationship that might impair their ability to uphold the fundamental principles.

Table 7.1 Examples of threats firms may face

Types of Threats	Examples
Self-interest	Direct financial interest in client, including loans or other significant business relationships, or entering into a contingency fee arrangement relating to the assurance engagement. Having a close business relationship with a client. Having access to confidential information that might be used for personal gain. Dependence on total fees from a client or concern about losing a significant client. Accepting gifts offered by client over a documented threshold. Discovery of a significant error from a previous professional service performed by the same firm
Self-review	A firm issuing an assurance report on the effectiveness of a system after designing or implementing that very system. A firm performing a service for an assurance client that directly affects the subject matter information of the assurance engagement. Accepting an engagement, the subject matter of which has been prepared by the firm.
Advocacy	Promoting shares in a listed audit client. Acting as an advocate on behalf of an assurance client in resolving disputes with third parties or in litigation. Lobbying in favor of legislation on behalf of a client.
Familiarity	Close or immediate family relationship with a director or officer of a client or with an employee who is in a position of influence over the subject matter of the engagement (applies to any member of the engagement team). A former engagement partner of the firm being a director or officer of the client, or an employee with direct and significant influence over the subject matter of the assurance engagement. An audit team member having a long association with the audit client.
Intimidation	Being threatened with dismissal or replacement in a client engagement because of a disagreement about a professional matter. Being threatened with litigation by a client. Feeling pressured to agree with the judgment of a client employee because the employee has more expertise on the matter in question. Being informed by a partner of the firm that a planned promotion will not occur unless the accountant agrees with an audit client’s inappropriate accounting treatment.

7.2.3b Evaluating Threats

When a threat to compliance with the fundamental principles or independence is identified, the practitioner will evaluate whether such a threat is at an acceptable level. An acceptable level is a level at which the practitioner, using the reasonable and informed third party test, would likely conclude that the practitioner complies with the fundamental principles.

The practitioner will consider the qualitative as well as the quantitative factors when evaluating the level of threats. Also, the practitioner will take into account the combined affect of multiple threats, if applicable.

In addition to helping to identify threats, the existence of certain conditions, policies and procedures established by the profession, legislation, regulation, the firm or the client might also be factors relevant in evaluating the level of threats to compliance with the fundamental principles. These conditions, policies and procedures are no longer categorized as safeguards because they are not specific actions the practitioner or firm takes to reduce threats to an acceptable level and, therefore, do not meet the new criteria needed to be considered a safeguard. Nevertheless, their existence, or lack thereof, should be considered by the practitioner in determining whether they contribute in reducing the threat to an acceptable level.

7.2.3c Addressing Threats

If the practitioner determines that the threats identified are not at an acceptable level, the practitioner must address the threats by eliminating them or reducing them to an acceptable level. To address threats that are not at an acceptable level, the practitioner has three possible courses of action:

a) Eliminating the circumstances, including interests and relationships, that have created the threats;

b) Applying safeguards, where available and capable of being applied, to reduce the threat to an acceptable level; or

c) Declining or ending the specific professional activity.

Depending on the facts and circumstances, a threat might be addressed by eliminating the circumstance creating the threat. However, there are some situations where threats can only be addressed by declining or ending the professional activity. This is because the circumstances that created the threats cannot be eliminated or safeguards are not capable of being applied to reduce the threat to an acceptable level.

7.2.3d Safeguards

It is important to be aware of the safeguards that can be put in place to reduce threats to an acceptable level. Safeguards are actions, individually or in combination, that the practitioner can take that effectively reduce threats to compliance with the fundamental principles to an acceptable level. Actions are safeguards only when they are effective in reducing threats to an acceptable level such that the practitioner complies with the fundamental principles. The practitioner needs to exercise professional judgment to determine whether an action is a safeguard.

Examples of safeguards

Safeguards vary depending on the facts and circumstances. Examples of actions that, in certain circumstances, might be safeguards to address threats include:

- Assigning additional time and qualified personnel to required tasks when an engagement has been accepted might address a self-interest threat
- Having a professional accountant who was not involved with the non-assurance service review the non-assurance work performed might address a self-review threat;
- Having an appropriate reviewer who was not a member of the assurance team review the assurance work performed or advise as necessary might address a self-review threat;
- Using different partners and engagement teams with separate reporting lines for the provision of non-assurance services to an assurance client might address self-interest, self-review, advocacy, familiarity or intimidation threats;
- Separating teams when dealing with matters of a confidential nature might address a self-interest threat;
- Disclosing the nature of services provided and the extent of fees raised to those charged with governance of the client might address a self-interest threat; and
- Involving another firm to perform or re-perform part of the engagement might address self-interest, self-review, .advocacy, familiarity or advocacy threats.

Ethics Threats and Possible Safeguards

The IESBA Code provides an overview of the types and examples of ethics threats and the example of safeguards that might address these threats. These are noted in Table 7.2 together with the relevant section of the IESBA Code.

Table 7.2 Possible threats and safeguards

Professional Appointment (Section 320 of the Code)		
Stage	*Possible threats*	*Safeguards that might be applied*
Client acceptance	Questionable management conduct (for example, involvement with illegal activities, money laundering, dishonesty or questionable financial reporting practices) might create self-interest threats	Obtain thorough knowledge and understanding of client and its governance structures. Secure client's commitment for corporate governance practices and internal controls.
Engagement acceptance	Lack of adequate skills and knowledge to carry out engagement might create self-interest threats Reliance on improper or inadequate advice might also create self-interest threats	Use experts where necessary. Agree on realistic time frame for the performance of the tasks. Assign sufficient and experienced employees with necessary competencies. Where reliance on an expert is necessary, ascertain their reputation, expertise, resources and applicable professional and ethical standards.

Professional Appointment (Section 320 of the Code)		
Stage	*Possible threats*	*Safeguards that might be applied*
Changes in professional appointment	Self-interest threats might be created by the following facts and circumstances: • Rationale for changes in professional appointment not fully known, leading to uninformed decision to accept • Request to perform complementary or additional professional work to the existing work of another professional accountant where there is a lack of or incomplete information • The professional appointment is constrained by an issue of confidentiality or prohibition by legal regulation in obtaining information	Contact the existing accountant before acceptance. Ascertain the reasons behind change. Request information on any facts that in the opinion of the existing accountant, the proposed accountant needs to be aware of. Request the disclosure of information through the client from the existing accountant. Discuss with the client in order to obtain confidential information from existing accountant. Inquire of third parties or background investigations of senior management or those charged with governance of the client.

Conflicts of interest (Section 310 of the Code)	
Possible threats (business relationships)	*Safeguards that might be applied*
The professional accountant competes directly with client or is in a joint venture with a major competitor of a client Professional services for clients whose interests are in conflict or in dispute with each other in relation to the matter in question	Notify client of the firm's business interest that may present a conflict of interest and obtain their consent to act. Notify all known relevant parties that the professional accountant is acting for two or more parties in respect of a matter where the respective interests are in conflict and obtain their consent to act. Notify the client that the professional accountant does not act exclusively for any one client in the provision of the proposed services and obtain their consent to act. Other safeguards include: • The use of separate engagement teams; • Clear guidelines for members of the engagement team on issues of security and confidentiality; and • Having an appropriate reviewer, who is not involved in providing the service or otherwise affected by the conflict, review the work performed to assess whether the key judgments and conclusions are appropriate.

Second Opinions (Section 321 of the Code)	
Possible threats (business relationships)	*Safeguards that might be applied*
Providing a second opinion on the application of accounting, auditing or other reporting standards on behalf of a company that is not an existing client, especially when it is not based on the same set of facts might create a self-interest threat	Obtain client permission to contact the existing accountant, describing the limitations surrounding the second opinion with the client and providing the existing accountant with a copy of the opinion.
Fees and other types of remuneration (Section 330 of the Code)	
Possible threats (business relationships)	*Safeguards that might be applied*
Lowballing: a self-interest threat to professional competence and due care when fees quoted are lower than the amount required to perform a competent service	Adjusting the level of fees or scope of the engagement. Having an appropriate reviewer review the work performed.
Contingency fees: a self-interest threat to objectivity, especially on non-assurance engagement	Obtain advance written engagement letter with the client regarding the basis of remuneration. Have an appropriate reviewer review the work performed.
Referral fee or commission received will create a self-interest threat to objectivity, professional competence, and due care	Disclose to the client any arrangements to pay a referral fee to another professional accountant for the work referred. Disclose to the client any arrangements to receive a referral fee for referring the client to another professional accountant. Obtain advance agreement from the client for commission arrangements in connection with the sale by a third party of goods or services to the client.

Inducements, Including Gifts and hospitality (Section 340 of the Code)	
Possible threats	*Safeguards that might be applied*
Accepting a gift from a client creates a self-interest threat or familiarity threat; an intimidation threat to objectivity may also result from the possibility of such offers being made public	Being transparent with senior management of the firm or of the client about offering or accepting an inducement. Registering the inducement in a log monitored by senior management of the firm or another individual responsible for the firm's ethics compliance. Having an appropriate reviewer, who is not otherwise involved in the professional service, review any work performed or decisions made by the practitioner or firm with respect to the client from which the practitioner accepted the inducement. Donating the inducement to charity after receipts and appropriately disclosing the donation, for example, to a member of senior management of the firm. Reimbursing the cost of the inducement received. As soon as possible, returning the inducement, such as a gift, after it was initially accepted.

Relationships – Business, Family and Personal, Recent Service With an Audit Client, Serving as a Director or Officer of an Audit Client, Employment With an Audit Client, Temporary Personnel Assignments (Sections 520, 521, 522, 523, 524 and 525 of the Code)	
Possible threats	*Safeguards that might be applied*
Having interests in, or personal or business relationships with, a client or its directors, officers, or employees might create self-interest, familiarity or intimidation threats.	Remove the individual creating the threat from the engagement team. Structure the responsibilities of the audit team so that any audit team members do not deal with matters that are within the responsibility of a close family member. Having an appropriate reviewer review the work performed by an audit team member. In the case of an audit team member takes employment with a client is to have an appropriate reviewer review any significant judgments made by the individual while on the audit team.

7.2.3e Remaining Alert

If the practitioner becomes aware of new information or changes in facts and circumstances that might impact whether a threat has been eliminated or reduced to an acceptable level, the practitioner must re-evaluate and address the threat accordingly.

7.2.3f Consideration of Significant Judgments Made and Overall Conclusions

When addressing threats, the practitioner must form an overall conclusion about whether or not the actions they have taken, or intend to take, will eliminate the threats or reduce them to an acceptable level. This new requirement is referred to as the "step-back" provision. It also provides that the practitioner will make an overall assessment as to whether the significant judgments made or conclusions reached were appropriate, using the reasonable and informed third party test.

7.3 Risk Management within the Firm

7.3.1 Identifying Risk within an Accounting Firm

Risk management is an area of life within a firm that has increased in importance over the last few years. There are a number of reasons it is essential for a firm to have a risk management program in place, including:

- To protect the assets, finances and firm operations;
- To contribute to satisfactory legal compliance, corporate governance and due diligence;
- To improve the services offered by the firm;
- To protect the reputation, credibility and status of the firm; and
- To enhance confidence in the firm.

Implementing a risk management program provides many benefits to accounting firms. These include:

- More effective strategic planning in their firms;
- Better cost control through better workflows and client evaluation and engagement processes;
- Increased profitability through better client and job controls;
- Reduced risks of litigation as a consequence of better processes and contingency plans;
- Increased knowledge and understanding of exposure to risk;
- A systematic, well-informed and thorough method of decision-making;
- Less disruption and less rework through better understanding of process by all staff in the firm; and
- Sets the scene for continual improvement within a firm.

7.3.1a Establishing a Risk Management Program

In order to establish a risk management program, it is important to understand the steps involved. These steps are:

1. **Implement a risk management framework based on the risk policy**
2. **Establish the context**
    (a) Consider the goals and objectives of the firm;
    (b) Consider the environment within which the firm operates; and
    (c) Identify internal and external stakeholders.
3. **Identify risks**
    (a) Identify existing and potential risks as well as existing controls.

4. **Analyze and evaluate risks**
   (a) Analyze and evaluate your own firm's risks on a continuing basis; and
   (b) Identify high and low risks.
5. **Treat and manage risks**
   (a) Develop strategies to manage the identified risk.
6. **Communicate and consult**
   (a) Communicate and consult with all parts of the firm, as well as outside parties, to ensure that all are kept well informed.
7. **Monitor and review**
   (a) Monitor and review the risk management strategies on an ongoing basis.
8. **Record**
   (a) Keep a written record of all policies and procedures, including documentation of the assessment process, major risks identified and the measures designed to reduce the impact of these major risks.

After completing this risk review, where an area of the firm has been identified as posing a high risk, you need to:

- Evaluate your ability to reduce the risk in terms of existing procedures;
- Adjust or reconsider that area and its development;
- Retrain or employ personnel to meet any staffing weaknesses;
- Review the engagement with clients in that area of your firm; and
- Apply risk management procedures.

It is also important that you consider risk management procedures such as:

- Clarity on the terms of the engagement;
- Advising the clients on the risks involved and ensuring that going forward both you and the client are in agreement on the level of risk to be managed (if you agree it is not to be (or cannot be) eliminated);
- Obtaining adequate insurance and controlling claims once they have occurred;
- Maintaining accurate and contemporaneous documentation;
- Ensuring timeliness of action and diary systems;
- Only practicing in those areas where there is sufficient expertise; and
- Implementing strict selection criteria for clients and consultants or agents used.

Questions you should ask yourself to identify risks and determine how to treat them follow. Please note that the following checklist should be used as a guide only and should be customized for the individual circumstances of each firm.

Establish the context

The risk management process requires the practitioner to consider matters such as those set out in Table 7.3 below:

Table 7.3 Matters to consider in terms of context

☐	What outcomes does the firm want to achieve?
☐	What is the environment in which the firm operates? (for example, cultural, legal and operational)
☐	Identify internal and external stakeholders. (for example, clients, personnel, consultants, agents, internal systems, third parties, suppliers, etc.)

In defining the relationship between the firm and its environment, including all stakeholders, identification is made of the practice's strengths, weaknesses, opportunities and threats.

This "strategic" plan will include financial, operational, competitive, political (public image and perception), social, cultural and legal aspects of the firm.

9. Identify risks

Once the context has been established, the potential risk factors or threats and the existing risk controls of the firm need to be identified. Potential risks in a firm can be categorized as:

a. Services performed;

b. Contract risk;

c. Acceptance or continuance risk; and

d. Performance risk.

A checklist has been established to review each of these areas of risk and is attached as Appendix 7.6 at the end of this module.

10. Analyze and evaluate risks

A practitioner should analyze and evaluate the firm's risks on a continuing basis. Risk evaluation takes into account the following (see Table 7.4):

Table 7.4 Analyzing and evaluating risks on a continuing basis

☐	A comparison of exposure levels against the predetermined tolerance level.
☐	Importance of the activity that is being risk-managed and its outcomes.
☐	Degree of control over the risk.
☐	Potential or actual losses that may arise from the risk.
☐	Benefits and opportunities presented by the risk.

There may be times when practitioners would like to identify the cost of the controls and their adequacy. There are a number of ways to evaluate this—the simplest model is to consider the likelihood of occurrence of an event and the consequences of that event, e.g., Risk = Likelihood x Consequence.

Consult with others, and use your experience to calculate the level of risk. It may be categorized as extreme, high, moderate or low. The risks should be ranked to establish management priorities.

Among other matters, the assessment process needs to canvass items shown in Table 7.5 below.

Table 7.5 Assessing level of risk

	Consideration	Comment/Action	Date Completed
1.	The firm's existing and anticipated areas of practice		
2.	The composition, experience, and expertise of the firm		
3.	The management and internal control procedures of the firm		
4.	The likelihood of being sued and the potential ambit of any claim		
5.	The process to assess new and existing clients		

Other approaches which may be used to analyze identified risks include checklists, judgments based on experience and records, flow charts, brainstorming, systems analysis and scenario analysis.

Many practitioners have procedural manuals, checklists and internal processes already in place. The level of risk analysis undertaken will depend on the information and data available. It can range from qualitative, semi-quantitative, to quantitative. In the case of quantitative analysis, a sensitivity analysis should also be used to test the data being used.

When assessing the kind of risks the firm is exposed to, it is important to consider both the internal risks and the external risks. These two areas of risk are set out in more detail below.

7.3.2 Examining Internal Risk

7.3.2a Risks Posed by Staff

The practitioner should consider whether employees see the firm as a short-term employment option or a long-term opportunity.

The risk lies in the perception of the firm as a short-term employer. High staff turnover could result in disruption to the practice, and generate the expense of finding and training new staff who won't deliver a return to the firm if they also leave after a short time.

The practitioner should also consider whether there are employees in the firm who are critical to its success. If an employee is critical to the firm's success, billings and profits may suffer if that employee leaves the firm, sets up a practice in competition, or goes to work for a competitor.

The practitioner also needs to consider whether staff face occupational health and safety risks. If staff members work in an unsafe environment, the firm is at risk for fines and penalties and the absenteeism, injury or even the death of an employee.

Risk mitigation strategies for these types of risks include:

- Implementing selection procedures that increase the probability of finding the right staff for the firm, those who take a longer-term view;

- Putting in place confidentiality agreements and/or reasonable restraint of trade agreements to be signed by key staff, or all staff where appropriate;
- Implementing a robust performance development system for communicating performance expectations and goals, monitoring performance and setting remuneration;
- Providing ongoing training and cross-training for staff, consistent with the needs of the firm;
- Allocating several people to fulfill key tasks and provide backup in the event of illness or sudden departure;
- Rotating employees through various functions of the practice to familiarize them with other areas of the firm;
- Implementing suitable occupational health and safety policies to minimize risks;
- Using equity interests, profit-sharing or other incentives to help retain key personnel and let them share in the success they create for the practice. But be careful how such incentives schemes are designed, as they could encourage unintended behavior; and
- Reviewing the period of notice required of staff who resign. Be careful with this, as it could have unintended legal consequences, depending on your local regulations.

7.3.2b Risks Posed by the Business Premises and its Location

The practitioner needs to consider how dependent the firm is on its current location.

If the firm depends significantly on where it is located to generate billings, moving the premises away from the current location may cause disruption by affecting customer, staff and supplier access. Another risk is that, in the event of a fire, flood or other disaster, the business may not be able to restart trading if the premises, equipment, materials and/or records are destroyed.

Another matter for the practitioner to consider is whether the business is growing, or is relatively stable. If it is growing strongly, the practitioner will need to consider how long this can be expected to continue and how big the premises will need to be in two, five or ten years' time.

Unless plans have been made to expand the current premises, the risk is that the business may not be able to grow to its full potential, and it could stagnate or be overtaken by competitors.

Risk mitigation strategies for the above risks include:

- Identifying a number of suitable alternative premises which would suit customers, suppliers and staff;
- Where the premises suit the business's long-term needs, consider securing a long-term lease or right of first option when the lease expires; and
- Managing the business to predict future space requirements early.

7.3.2c Threats to Goodwill and Reputation

An important matter for the practitioner to consider is how exposed the firm is to a threat to its reputation or goodwill. For example, what would happen if the firm provided bad advice, or was involved in a major fraud?

The risk is that a fraud, or other similar event, would be likely to generate bad publicity. This could cause immediate distress to the firm and possibly also cause longer-term damage to its goodwill and reputation.

Risk mitigation strategies would include:

- Incorporating robust review processes and quality assurance systems to avoid a situation that may damage the firm's reputation;
- Investing in research and development and keeping up-to-date with technological advances; and
- Compulsory training and development programs for staff.

7.3.2d Risks Posed by Information Technology

The important issue to consider here is the extent to which the firm relies on information technology (IT). The level of risk created by using IT increases as the firm becomes more reliant on it.

The obvious risk is that if the firm is heavily reliant on IT, it might not be able to operate without it—for example, if the main server or processor fails during a high-usage period. There are many other risk areas associated with IT and cloud solutions, including:

- IT service delivery: do all the software applications (including spreadsheets) work as intended? Are they all accurate?
- IT solution delivery: do you try to integrate IT solutions into daily work processes, so that the firm runs more efficiently and predictably?
- IT benefit realization: consider not only the cost of an application, but also consider the cost of not implementing that application. Some IT outlays are essential simply to keep pace with others in the industry.

Risk mitigation strategies include:

- Protecting laptops and desktops;
- Keeping data safe by performing backups and storing those backups off-site;
- Ensuring software licenses are up-to-date;
- Ensuring software update versions are run on a regular basis;
- Having documented Internet access strategies;
- Establishing and monitoring social media use policies;
- Protecting networks;
- Protecting servers;
- Securing the line of business applications;
- Ensuring appropriate IT support is available within an acceptable time frame;
- Having an uninterrupted power supply unit; and
- Conducting appropriate IT training for staff.

Policies and Checklists for technology risk management strategies are included in Module 5.

7.3.3 External Risk

7.3.3a Risks Posed by Customers

An important matter for the practitioner to consider is whether the firm is highly dependent on a small number of major clients. For example, is there one client, or client group, who generates 65% or more of total revenue?

The risk is that if the firm relies on a small number of major clients, profit and cash flow may be affected in the short term if one of them leaves the firm, or stops yielding revenue.

Risk mitigation strategies include:

- Locking in major clients through long-term service contracts, regularly visiting them, or continually asking their views about the firm's services;
- Spreading the risk by developing smaller existing customers so they become larger customers;
- Seeking new, profitable customers; and
- Finding lower-cost ways of servicing the less profitable customers.

7.3.3b Risks Posed by Competitors

Virtually every business has competitors. However, if competitors—both current and potential—pose a significant threat to the practice, then the viability of the firm is at risk. The practitioner needs to consider whether their competitors pose a threat.

Risk management strategies include:

- Continuing to build on relationships with clients and the local community (providing great service as a way of combating competitors!);
- Researching industry trends, and adopting new services or ways of delivering those services;
- Investing in the development of new services; and
- Continually monitoring competitors, including the prices they charge.

7.3.4 Developing a Risk Framework for Your Firm

When assessing your firm for sources of risk, you should consider the following areas:

- Integrity;
- Services offered;
- Marketing and communication;
- Staff and human resources issues;
- Information and resource management;
- Regulatory obligations and intervention;
- IT issues and security;
- Management collapse (succession planning);
- Acceptance and continuance of clients; and
- Cash flow management.

Figure 7.1 shows these in diagram form.

Figure 7.1 Sources of risk for an accountancy firm

Each of these areas should be considered as you develop your firm's risk framework.

A series of checklists has been established to review each of these areas of risk and is attached as Appendix 7.6 at the end of this module, covering:

- Integrity;
- Services offered;
- Marketing and communication;
- Staff and human resources;
- Information and resource management;
- Regulatory obligations;
- Information technology and security;
- Management collapse and succession planning;
- Acceptance or continuance of clients; and
- Cash flow management.

Note that these checklists are suggested as a guide only and should be amended to suit the specific needs of your firm. Also be aware of any local regulatory impact.

7.3.5 Adopting Risk Mitigation Strategies

Strategies need to be developed to manage the risks you identify in your firm. Options can be selected from any of the following:

- Accept;
- Avoid;
- Transfer (in part or full);
- Reduce likelihood;
- Reduce consequences; and
- Retain the risk.

Where risks fall within the tolerance level of exposure, they may be treated as low-priority and retained. Optimal action plans are developed based on:

- Current levels of risk exposure;
- Benefits arising from actions/controls;
- The duration of time to implement actions; and
- Available budget.

7.3.5a Risk Management Strategies

There are numerous examples of strategies that can be used to manage risk. These include:

i. **Contingency strategy**: applies to risks of higher consequence but lower likelihood of occurrence and aims to bring the potential consequence of the risk within acceptable confines. Simple examples of such a risk control strategy are insurance and contractual indemnities, business continuity plans and contracting some or all of the activity to another organization or person.

ii. **Preventative strategy**: applies where potential impacts are not very large but the likelihood of occurrence is high, for example, client complaints. In this case, quality control assurance procedures, supervision and training would be instances of this strategy.

iii. **Monitoring strategy**: is suited to exposures where the likelihood and consequence of risk are deemed to be relatively small. This strategy aims to ensure all "standard safeguards" are in place and working. It also requires the risk to be periodically reviewed. For example, quality checks, regular reporting, audit and performance reviews.

iv. **Mixed strategy**: corresponds to managing a risk environment; that is, managing potentially likely negative outcomes and outcomes of high impact or consequence which would involve a combination of strategies outlined above.

Where an area of the firm is identified as posing a high risk, the firm should follow actions suggested in Table 7.6.

Table 7.6 Strategies to manage risk

a.	Evaluate the firm's ability to reduce the risk in terms of existing procedures;
b.	Adjust or reconsider that area of the firm and its development;
c.	Retrain or employ personnel to meet any staffing weaknesses;
d.	Review the engagement with clients in that area of the firm; and
e.	Apply risk management procedures.

7.3.5b Risk Management Procedures

The IESBA Code outlines a number of important risk management procedures that need to be considered by the firm. These include:

1. The engagement letter

- Confirms acceptance of the appointment;
- Outlines the objective, scope and extent of the engagement;
- Highlights the extent of the member's responsibilities to the client;
- Defines the client's responsibilities;
- Manages the "client expectation gap," i.e., matching the services expected by the client with the services delivered;
- Confines the extent of exposure by:
  - specifying limitations on the work to be undertaken;
  - confining the advice to the client only;
  - restricting use of member's name on documentation supplied to the client;
  - obtaining an indemnity from the client, any third party or in connection with receiverships, trust and secretarial work; and
- Sets the fees applicable to the engagement.

A letter of engagement is an essential document in any firm and benefits both the practitioner and the client. It is covered in greater detail in Section 7.4 of this module.

Documented policies for accepting a new client or parting with an existing client are essential to mitigate risk.

2. Advise clients on risks

To avoid having to assume responsibility for the client's risk-taking, advise the client in writing of relevant dates and consequences in the event of failure by the client to act. This will transfer the risk of noncompliance back to the client to act and/or follow-up.

3. Accurate and contemporaneous documentation

It is recommended that all advice a member of staff provides be noted in a file/diary system, or by confirmation letter or report to the client. The information that should be included is:

- Date;
- Time;
- Content of conversation/advice;
- Notation to whom it was made; and
- Signature (if applicable).

4. Timeliness of action and diary systems

File notes will have the dual effect of:

- Assisting with the recollection of events if there is litigation many years later; and

- Being tendered in Court as evidence that a conversation actually occurred (subject to authenticity of documentation being established).

5. Practice in areas where there is sufficient expertise

Each staff member should recognize his or her own limitations. If the staff member forms the view that there is insufficient time or he or she does not have the skill required to perform the service requested, then the matter should be referred on to a specialist.

6. Client selection

A review of the firm's client mix is recommended with a view to considering increasing the proportion of clients requiring lower-risk advice. The review should examine:

- type of business conducted by the client;
- ongoing work or one-time engagement; and
- effect of economic climate on client's business.

It is important to note that the application of such measures does not relieve the member of the duty to exercise the level of skill, care and judgment appropriate to the service provided, and therefore application of the highest standard at all levels is essential.

Generally, the firm should consider its quality control and assurance procedures, the problems that have arisen, and how they have been dealt with in the past.

7. Monitoring

A firm needs to continuously monitor and review the strategies used to manage risk.

It is also necessary to monitor and manage the implementation of the action plan against time and budget.

Over time, new risks are created, existing risks are increased or decreased, risks no longer exist, the priority of risk may change or the risk treatment strategies may no longer be effective.

Monitoring should comprise:

- Monitoring existing risks
- Identifying new risks
- Identifying any trouble spots
- Evaluating the effectiveness of current risk treatment strategies.

Monitoring ensures that new measures are introduced to control new risks as these emerge. Ongoing review is required to ensure that strategies remain relevant, and that the overall risk control position is relative to the potential costs of the risk.

8. Communication and consultation

The risk management process requires continuous communication and consultation with all parts of the practice as well as with outside parties to ensure that all personnel are informed of all stages of the process.

9. Record-keeping

All policies and procedures should be in writing. Records should be maintained documenting the assessment process carried out, the major risks identified and the measures recognized to reduce the impact of these major risks.

Failure to document policies can lead to breaches in performance due to misunderstanding or misinterpretation. A written set of policy statements supplied by documented procedures provides a constant reference, a guide to action and a framework for checking that the operations are conducted in the manner intended by the firm.

7.4 Client Engagement

7.4.1 The Engagement Process

The relationship between a practitioner and a client is an important one to both parties. As already discussed, the practitioner brings a number of important elements to the relationship. These should include integrity, objectivity, professional competence and due care, confidentiality and professional behavior. In addition to these characteristics, the practitioner also brings individual interpersonal skills to the relationship.

One of the most important aspects of the professional relationship is a clear understanding of what the relationship is about; what specifically it is that the client has engaged the practitioner to do. The formal way of acknowledging this is in the form of an engagement letter, or engagement document. This is where the practitioner provides a formal, written understanding of what the client is seeking.

Such a letter confirms the arrangement—or provides the opportunity to clarify any uncertainties—which may exist between the client and the practitioner. It goes a long way toward avoiding client disputes, as the terms of the engagement are clearly stated up front in a clear and explicit manner. This may not always be the case, but without an engagement letter, the practitioner is in a weakened position.

7.4.1a Terms of Engagement for Professional Services

The engagement letter is one way of formalizing the relationship between practitioner and client. The process of documenting and communicating the terms of the engagement should ensure that there is a clear understanding between the client and the practitioner regarding the terms of engagement. It is in the interests of both the client and the practitioner that this occurs, preferably before the engagement commences, to avoid misunderstandings with respect to the engagement.

The terms of engagement do not need to take the form of a letter or agreement. For example, a standard format handout, brochure, leaflet or electronic communication is also acceptable. However, any form of agreement that is not signed by both parties poses a higher risk than a signed letter of engagement, contract, or agreement.

The law establishes the objectives and scope of some engagements. It should be noted that documentation of the terms of engagement cannot reduce those obligations imposed by law. Where the engagement is undertaken under legislation, the practitioner should refer to the applicable provisions of the law in the engagement letter or document.

7.4.1b General Contents of an Engagement Document

The following is a guide to matters that the practitioner may wish to consider for inclusion in an engagement letter. Examples of the types of matters you may wish your firm to consider include:

Purpose: The engagement document should explain that its purpose is to set out and confirm the understanding of the practitioner of the terms of the engagement.

Objectives of the engagement: A brief summary of the objectives of the engagement, including reference to the fact that:

- Procedures to be performed will be limited exclusively to those related to the engagement;

- Neither an audit nor a review will be conducted, and, accordingly, no assurance will be expressed (if applicable); and
- Unless otherwise agreed, the engagement cannot be relied upon to disclose irregularities, including fraud, other illegal acts and errors that may occur.

Scope of the engagement: Pertinent details of such matters as:

- Time periods covered by the engagement;
- Period of appointment and time schedules;
- References to any legislation and professional standards that may be relevant to the engagement;
- Client operations or procedures to be included in the engagement;
- Details of information to be provided by the client;
- Due diligence directly connected to the anti-money laundering and other corruption legislation in the jurisdiction(s) in which the client is operating;
- Any limitations on the conduct of the engagement; and
- Other matters considered necessary or appropriate.

Engagement output: Details of reports or other anticipated outputs, including:

- Expected timing;
- Intended use and distribution of reports; and
- Nature of any anticipated disclaimer or arrangement that limits the liability of the practitioner, including appropriate limitation of liability clauses for those practitioners participating in legislative schemes which limit their liability with respect to the client or any other user of the results of the engagement.

Relative responsibilities: Responsibilities agreed upon, detailing those acknowledged as the responsibility of:

- the practitioner, including reference to relevant confidentiality requirements and the impact of them on the quality review program of the relevant professional body to which the practitioner belongs;
- the client, noting the fact that the client is responsible for the completeness and accuracy of information supplied to the practitioner; and
- any third party.

Involvement of other members in public practice: Where the work of another practitioner is to be used on some aspects of the engagement, the details of this involvement should be documented in the engagement document.

Fees and billing arrangements: Reference to the basis of fees (e.g., time-based billing, fixed price contracts, contingent fee arrangements or other similar agreement). Details of agreed-upon billing schedules should also be included.

Ownership of documents: The engagement document should make clear who owns any documents produced as a result of the engagement or provided by the client for such a purpose, including electronic data. If a firm has a policy of seeking to exercise a right of lien over such documents in the event of a dispute with a client, this policy should be disclosed in the engagement document communicated to the client, including the procedure for dealing with disputes over the lien.

Confirmation by the client: Request for a response from the client confirming its understanding of the terms of engagement as outlined in the engagement document. It is preferable for this confirmation of client acceptance to be obtained in a written form.

7.4.2 Review and Re-Engagement

Practitioners should be aware of the importance of reviewing their relationships with their clients to ensure that they are satisfied with the service they are currently receiving. This also provides the client with the opportunity to offer feedback, if needed, on how the accounting firm can improve its services. It also provides the practitioner with the opportunity to discuss new or additional services that may be relevant to the client.

In light of this, the firm should establish policies and procedures for the acceptance and continuance of client relationships and specific engagements. These should be designed to provide reasonable assurance that the firm will only undertake or continue relationships and engagements where it:

- Has considered the integrity of the client and does not have information that would lead it to conclude that the client lacks integrity;
- Is competent to perform the engagement and has the capabilities, time and resources to do so; and
- Can comply with ethical requirements.

The firm should obtain the information it considers necessary before accepting an engagement with a new client, when deciding whether to continue an existing engagement, and when considering acceptance of a new engagement with an existing client. Where issues have been identified, and the firm decides to accept or continue the client relationship or a specific engagement, it should document how the issues were resolved.

With regard to the integrity of a client, matters which the firm should consider include, for example:

- The identity and business reputation of the client's principal owners, key management, related parties and those charged with its governance. Specific requirements may be required by law in some jurisdictions.
- The nature of the client's operations, including its business practices.
- Information concerning the attitude of the client's principal owners, key management and those charged with its governance toward such matters as aggressive interpretation of tax regulations, accounting standards, and the internal control environment.
- Whether the client is aggressively concerned with maintaining the firm's fees as low as possible.
- Indications of an inappropriate limitation in the scope of work.
- Indications that the client might be involved in money laundering or other criminal activities. Very specific requirements may be required under Anti-Money Laundering or Counter Terrorism Financing Law (AML/CTF) in some jurisdictions.
- The reasons for the proposed appointment of the firm and non-reappointment of the previous firm.

Module 3 of this guide discussed the process a firm should undertake when assessing prospective clients and whether they would represent a good fit for the firm. The process of client review also gives the firm the opportunity to reassess their level of interest in retaining the client.

Table 7.7 provides useful guidance when assessing whether to continue servicing current clients of the firm:

Table 7.7 Reviewing clients of the firm

	Question	Answer/Comment
1.	Do the management and staff of the firm like working with the client?	
2.	Does the client respect the firm, its opinion, its work and its management and staff?	
3.	Does the client represent a risk to the firm?	
4.	Do the firm's management and staff relate well to the client?	
5.	Does the client relate well to the firm and the firm's team?	
6.	Does the client utilize a number of the firm's services?	
7.	Does the client pay bills on time?	
8.	Does the client work cooperatively with the firm when required?	
9.	Does the client cause the firm's management and staff stress?	
10.	Is there a good fit culturally?	
11.	Does the firm add value to the client's business?	
12.	Does the client add value to the firm?	
13.	Is the firm proud to introduce the client as such?	
14.	Is the client proud to introduce the firm as its accountants?	
15.	Does the client observe ethical business principles?	
16.	Has the client asked the firm to compromise the practice's ethical values?	
17.	Are there other ways of servicing this client?	
18.	Has an annual client assessment been undertaken to ensure client represents value for money in terms of income based on their risk profile.	

7.4.3 Reviewing Ongoing Engagements

As mentioned above, the review and re-engagement of clients provides the practitioner with the opportunity to meet and discuss work performed to date with the client. It not only provides the opportunity for the client to discuss how the practitioner could improve their service, but also allows the practitioner the opportunity to discuss with the client areas in which they can improve the way they deal with the practitioner.

For recurring engagements, the practitioner may decide not to send an engagement letter on each occasion. The following factors may affect this decision:

- Any indication that the client misunderstands the objectives and scope of the engagement;
- Any significant changes in the terms of the engagement;
- A recent change of client management or ownership;
- A significant change in the nature or size of the client's business; or
- Legal requirements.

Any of these factors may cause the practitioner to consider issuing a new or revised engagement letter.

7.4.4 Managing the Disengagement Process

It is a fact of life in an accounting firm that relationships with clients will sometimes come to an end. This may come about because you want the client to leave, or if—for any number of reasons—the client chooses to go to another firm.

You may receive a professional letter from the new accountant who has been engaged, advising you of their appointment. It is recommended that you acknowledge their letter and provide whatever details they request, within your policy guidelines.

Unless the client has contacted you already, you may wish to contact the client to let them know you have received the professional letter from the other accounting firm and that you will act accordingly.

You may wish to engage in a discussion with the client as to the reasons for their leaving. This may provide you with important feedback on your firm. If you approach it with the right attitude, you may discover a systemic problem in your firm that needs to be addressed.

The firm should establish policies and procedures for those occasions when it withdraws from an engagement or from both the engagement and the client relationship. It should include consideration of issues including the following:

- Discussing with the appropriate level of the client's management and those charged with its governance the appropriate action that the firm might take based on the relevant facts and circumstances.
- If the firm determines that it is appropriate to withdraw, discussing with the appropriate level of the client's management and those charged with its governance withdrawal from the engagement or from both the engagement and the client relationship, and the reasons for the withdrawal.
- Considering whether there is a professional, regulatory or legal requirement for the firm to remain in place, or for the firm to report the withdrawal from the engagement or from both the engagement and the client relationship, together with the reasons for the withdrawal, to regulatory authorities.
- Documenting significant issues, consultations, conclusions and the basis for the conclusions.
- Have all legislative or professional requirements around the disengagement of clients been adhered to.

7.5 Quality Control Processes within an Accounting Firm

7.5.1 Objective of Quality Control

Quality control is an important component of any strategy for delivering consistent, high-quality services to clients. Quality control encompasses the firm and its objectives, the services provided, the delivery of those services, the quality of the work, the processes and policies adopted, and the staff and management.

A system of quality control essentially consists of policies designed to achieve the objectives of the firm and procedures necessary to implement and monitor compliance with those policies. Professional accounting firms also need to ensure that the quality of their work meets professional standards. A quality control system means they have documented what they do and how they do it.

The relevant minimum standards for quality control are:

- 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* issued by the IAASB;

- International Standard on Auditing (ISA) 220, *Quality Control for an Audit of Financial Statements* issued by the IAASB; and
- *International Code of Ethics for Professional Accountants (including International Independence Standards)* issued by the IESBA.

The *Guide to Quality Control for Small- and Medium-Sized Practices*, which provides guidance on implementing ISQC 1, can be downloaded.

7.5.2 Benefits of an Effective Quality Control System

An effective quality control system reduces the risk of error, thereby reducing exposure to complaints from clients and possible litigation or professional indemnity claims. It is also important in demonstrating that appropriate standards have been followed in the event of any litigation or professional indemnity claims. Other benefits offered by an effective quality control system include:

- Enhanced reputation and brand value in the marketplace;
- Enhanced risk management;
- Improved client relationships;
- Improved recruitment and retention of employees; and
- Improved efficiencies in the provision of services.

7.5.3 General Principles of Quality Control

Quality control systems for professional accounting practices are essentially based on ISQC 1 (the standard). This states that a system of quality control consists of policies and procedures designed to achieve two objectives. A firm can have reasonable assurance that:

- The firm and its personnel comply with professional standards and regulatory and legal requirements; and
- Reports issued by the firm, or engagement partners, are appropriate in the circumstances.

The system of quality control is to include policies and procedures that address each of the following:

- Leadership responsibilities for quality within the firm;
- Ethical requirements;
- Acceptance and continuance of client relationships and specific engagements;
- Human resources;
- Engagement performance; and
- Monitoring.

The quality control policies and procedures are to be documented and communicated to all staff. They should include a full description of the relevant policies and procedures and outline the objectives they are designed to achieve. It should also be made clear that each staff member has a personal responsibility for quality control and is expected to comply with the firm's policies and procedures.

The firm should also recognize the importance of obtaining feedback on its quality control system from staff, encouraging communication of staff views or concerns on quality control matters.

The nature of the policies and procedures developed by individual firms will depend on various factors, such as the size and operating characteristics of the firm. They do not need to be complex or time-consuming to be effective, but it is important for firms to establish policies and procedures that are both relevant and proportionate to the size of their practice.

7.5.4 Quality Control Elements

7.5.4a Leadership Responsibilities for Quality within the Firm

Your firm should aim to establish policies and procedures that promote an internal culture which recognizes that quality is essential in performing client engagements. These policies and procedures will require you to assume ultimate responsibility for the quality control system of the practice.

The example you set will significantly influence the culture of the firm. Promoting a quality-oriented culture depends on clear and consistent actions and messages from all staff. Such deeds and attitudes encourage a culture that recognizes and rewards high-quality work. Training seminars, formal or informal meetings, mission statements, newsletters, or briefing memoranda may communicate this message. It can be incorporated in the firm's internal documentation and training materials. It can also be included in staff appraisals in a way that supports and reinforces the firm's view on the importance of quality and how it is to be achieved in a practical sense.

7.5.4b Relevant Ethical Requirements

The firm is to establish policies and procedures designed to provide it with reasonable assurance that the firm and its staff comply with relevant ethical requirements.

The relevant ethical requirements are based on the fundamental principles contained in the professional standards, which include:

- Integrity;
- Objectivity;
- Professional competence and due care;
- Confidentiality; and
- Professional behavior.

In order to comply with these ethical requirements, the firm must have policies and procedures in place to identify and evaluate those circumstances where these requirements are under threat. It must then outline the appropriate action to eliminate those threats, or reduce them to an acceptable level so that compliance is not compromised.

It is therefore necessary to identify any actual or perceived conflicts of interest between your firm and your clients. The trust and confidence of clients is crucial to any ongoing professional relationship and avoiding real, potential or perceived conflicts of interest builds trust. Included in Appendix 7.2 is a form to assist in this assessment.

The firm's policies and procedures addressing these ethical requirements must be communicated to all staff and you should reinforce them through education and training, monitoring and providing a process for dealing with noncompliance. It is important to continually review these protocols to take into account any change of circumstances, including staff changes, client acquisitions or structural changes such as mergers.

Compliance with the ethical principles that apply to all areas of a professional accounting firm require:

- All personnel to adhere to the relevant ethical requirements;
- The establishment of procedures to communicate independence requirements to firm staff and, where applicable, others subject to them;
- The establishment of procedures to identify and evaluate possible threats to the fundamental principles, and to take appropriate action to eliminate those threats, or reduce them to an acceptable level by applying safeguards; and
- At least annually, written confirmation of compliance with the firm's policies and procedures on independence from all firm personnel required to be independent by relevant requirements (see Appendix 7.3 for an example form).
- For assurance practices, it is particularly important to establish policies and procedures to deal with identifying threats to independence, criteria for determining the need for safeguards, and the reporting of any breaches in a timely manner. Parts 4A and 4B of the IESBA Code outline the requirements for independence when undertaking an assurance engagement.

7.5.4c Acceptance and Continuance of Client Relationships

The firm is to establish policies and procedures for the acceptance and continuance of client relationships and specific engagements. These are designed to provide the firm with reasonable assurance that it will only undertake or continue relationships and engagements where it:

- Has considered the integrity of the client and does not have information that would lead it to conclude that the client lacks integrity;
- Is competent to perform the engagement and has the capabilities, time and resources to do so;
- Can comply with legal and ethical requirements; and
- Has reached an understanding with the client regarding the services to be performed.

1. Client integrity

Factors to consider regarding the integrity of a client have been examined in 7.4.2 as part of the review and reengagement process.

2. Client continuation

It is also important for you to review existing clients to ensure that any significant changes in the client's operations, business environment, or their key personnel are identified and documented, where appropriate. These changes may affect on your ability to comply with ethical requirements, which includes having the necessary knowledge or expertise to handle all of the issues the client may now be exposed to.

7.5.4d Human Resources

The firm is to establish policies and procedures designed to provide it with reasonable assurance that it has sufficient personnel with the capabilities, competence, and commitment to ethical principles necessary to perform its engagements in accordance with professional standards and regulatory and legal requirements and to enable the firm to issue reports that are appropriate in the circumstances.

These policies and procedures are to address the following personnel issues:

- Recruitment;
- Performance evaluation;
- Capabilities;
- Competence;
- Career development;
- Promotion;
- Compensation; and
- The estimation of personnel needs.

Compliance with this element of quality control requires:

- Recruitment of staff of integrity with the capacity to develop the capabilities and competence to perform the firm's work;
- Identifying the capabilities and competencies possessed by personnel;
- Assigning personnel based on the knowledge, skills, and abilities required in the circumstances and the nature and extent of supervision needed;
- Having personnel participate in general and industry-specific continuing professional education and professional development activities; and
- Selecting for advancement only those individuals who have the qualifications necessary to fulfill the responsibilities they will be called on to assume.

The firm's performance evaluation, compensation and promotion procedures should give due recognition and reward to the development and maintenance of competence and commitment to ethical principles. In particular, the firm is to:

- Make staff aware of the firm's expectations regarding performance and ethical principles;
- Provide staff with evaluation of, and counselling on, performance, progress and career development; and
- Help staff understand that advancement to positions of greater responsibility depends on, among other things, performance quality and adherence to ethical principles. Failure to comply with policies and procedures may result in disciplinary action.

The size and circumstances of the firm will influence the structure of its performance evaluation process. Smaller firms, in particular, may employ less formal methods of evaluating the performance of their staff.

1. Recruitment and retention

The recruitment and retention strategy of the firm should include policies and procedures which cover:

- Position interview and evaluation procedures;
- Maintaining current job descriptions for all positions;
- Orientation of new personnel; and
- Ongoing professional development and training to ensure maintenance of professional and educational standards.

2. Assignment to engagements

As a practitioner, you should only take on engagements for which you are confident you have the necessary skills, knowledge and experience to competently complete the work. Staff should be assigned after taking into account the nature and complexity of the engagement and the staff's capabilities and competencies.

7.5.4e Engagement Performance

The firm is to establish policies and procedures designed to provide it with reasonable assurance that engagements are performed in accordance with professional standards and regulatory and legal requirements and to enable the firm to issue reports that are appropriate in the circumstances.

Through its policies and procedures, the firm is seeking to establish consistency in the quality of its performance on the engagement. This is often accomplished through written or electronic manuals, software tools or other forms of standardized documentation, and industry- or subject-matter-specific guidance materials where relevant. Matters addressed include the following:

- How individual staff members are briefed on the engagement to obtain an understanding of the objectives of their work;
- Processes for complying with applicable engagement standards;
- Processes of engagement supervision, staff training and coaching;
- Methods of reviewing the work performed, the significant judgments made and the form of report being issued;
- Appropriate documentation of the work performed and of the timing and extent of the review; and
- Processes to keep all policies and procedures current.

It is important that all members of staff working on the engagement understand the objectives of the work they are to perform. Appropriate teamwork and training are necessary to assist less experienced members of staff to clearly understand the objectives of the assigned work.

Supervision includes the following:

- Tracking the progress of the engagement;
- Considering the capabilities and competence of staff members, whether they have sufficient time to carry out their work, whether they understand their instructions and whether the work is being carried out in accordance with the planned approach to the engagement;
- Addressing significant issues arising during the engagement, considering their significance and modifying the planned approach appropriately; and
- Identifying matters for consultation or consideration by more experienced staff during the engagement.

Responsibilities for review are determined on the basis that more experienced staff review work performed by less experienced staff. Reviewers need to consider whether:

- The work has been performed in accordance with professional standards and regulatory and legal requirements;
- Significant matters have been raised for further consideration;
- Appropriate consultations have taken place and the resulting conclusions have been documented and implemented;

- There is a need to revise the nature, timing and extent of work performed;
- The work performed supports the conclusions reached and is appropriately documented;
- The evidence obtained is sufficient and appropriate to support the report; and
- The objectives of the engagement procedures have been achieved.

Policies and procedures also should require that consultation takes place when appropriate, for example, when dealing with complex, unusual, unfamiliar, difficult, or contentious issues. In these cases it is necessary that:

- Sufficient and appropriate resources are available to enable appropriate consultation to take place;
- The nature, scope, and conclusions of such consultations be documented; and
- The conclusions resulting from such consultations are documented and implemented.

In addition, a policy should establish criteria against which all engagements are to be evaluated to determine whether an engagement quality control review should be performed.

To comply with this element, the firm needs to establish and maintain policies to:

- Plan all engagements to meet professional, regulatory and legal requirements;
- Perform work and issue reports and other communications that meet professional, regulatory, and the firm's requirements;
- Require that work performed by other team members be reviewed by qualified engagement team members, which may include the engagement partner, on a timely basis;
- Require that differences of opinion be dealt with and resolved and documented;
- Require that all engagements are evaluated against the criteria for determining whether an engagement quality control review should be performed;
- Establish procedures addressing the nature, timing, extent, and documentation of the engagement quality control review; and
- Establish criteria for the eligibility of engagement quality control reviewers.

7.5.4f Completion of the Assembly of Final Engagement Files

The firm is to also establish policies and procedures for staff to complete the assembly of final engagement files on a timely basis after the engagement and relevant reports have been finalized.

7.5.4g Confidentiality, Safe Custody, Integrity, Accessibility and Retrievability of Engagement Documentation

The firm shall also establish policies and procedures designed to maintain the confidentiality, safe custody, integrity, accessibility and retrievability of documentation used for the engagement.

Relevant ethical requirements require staff to maintain at all times the confidentiality of information contained in engagement documentation, unless specific client authority has been given to disclose information, or there is a legal or professional duty to do so. Specific laws or regulations may impose additional obligations on staff to maintain client confidentiality, particularly where data of a personal nature are concerned.

Whether engagement documentation is in paper, electronic or other media, the integrity, accessibility or retrievability of the underlying data may be compromised if the documentation could be altered, added to or deleted without the firm's knowledge, or if it could be permanently lost or damaged. Accordingly, the firm is to design and implement appropriate controls for engagement documentation to:

- Enable the determination of when and by whom the engagement documentation was created, changed or reviewed;
- Protect the integrity of the information at all stages of the engagement, especially when the information is shared within staff or transmitted to other parties via the Internet;
- Prevent unauthorized changes to the engagement documentation; and
- Allow access to the engagement documentation by staff and other authorized parties as necessary to properly discharge their responsibilities.

7.5.4h Retention of Engagement Documentation

The firm is to establish policies and procedures for the retention of engagement documentation for a period sufficient to meet the needs of the practice, or as required by law or regulation.

The needs of the firm to retain engagement documentation, and the period of such retention, will vary with the nature of the engagement and the circumstances of the firm. For example, whether the engagement documentation is needed to provide a record of matters of continuing significance to future engagements. The retention period may also depend on other factors, such as whether local law or regulation prescribes specific retention periods for certain types of engagements, or whether there are generally accepted retention periods in the jurisdiction in the absence of specific legal or regulatory requirements. In the specific case of audit engagements, the retention period ordinarily is no shorter than seven years from the date of the auditor's report, or, if later, the date of the group auditor's report.

Examples of procedures that the firm may ordinarily adopt for retention of engagement documentation include those that:

- Enable the retrieval of, and access to, the documentation during the retention period, particularly in the case of electronic documentation, since the underlying technology may be upgraded or changed over time;
- Provide, where necessary, a record of changes made to the engagement documentation after the engagement files have been completed; and
- Enable authorized external parties to access and review specific engagement documentation for quality control or other purposes.

The firm is also to ensure that the quality control system remains relevant and operates effectively by monitoring and updating the system on a regular basis. It is important to maintain policies and procedures and keep them current to reflect changes in professional standards and regulatory and legal requirements.

7.5.4i Monitoring

The firm is to establish policies and procedures designed to provide it with reasonable assurance that the policies and procedures relating to the system of quality control are relevant, adequate, operating effectively, and complied with in practice. Such policies and procedures are to include an ongoing consideration and evaluation of the firm's quality control system, including a periodic inspection of a selection of completed assignments.

The purpose of monitoring compliance with quality control policies and procedures is to provide an evaluation of:

- Adherence by the firm to professional standards and regulatory and legal requirements;
- Whether the quality control system has been appropriately designed and effectively implemented; and
- Whether the firm's quality control policies and procedures have been appropriately applied, so that engagement outputs that are issued by the firm are appropriate in the circumstances.

Monitoring encapsulates all the other elements of quality control, as it ensures compliance with policies and procedures established for meeting the objectives of leadership, ethics, client acceptance and continuance, human resources, engagement performance, as well as the monitoring itself. However, review of engagements is only one aspect. Monitoring also requires documentation of the procedures and findings, and the communication of those findings.

It is important that the responsibility for the monitoring process be assigned to the practitioner, or to partners with sufficient and appropriate experience and authority to assume the responsibility.

Monitoring procedures consist of the following:

1. **Assessing the firm's compliance with its quality control policies and procedures**
    - Review selected administrative and personnel records pertaining to the quality control elements;
    - Review engagement working papers, reports, and clients' financial statements;
    - Discuss with the firm's personnel;
    - Summarize the findings from the monitoring procedures at least annually, and consider the systemic causes of findings that indicate that improvements are needed; and
    - Determine any corrective actions to be taken or improvements to be made with respect to the specific engagements reviewed or the firm's quality control policies and procedures.
2. **Communicating results of monitoring**
    - Communicate the identified findings to appropriate management personnel within the firm;
    - Communicate at least annually, to relevant engagement partners and other appropriate personnel, deficiencies noted as a result of the monitoring process and recommend appropriate remedial action; and
    - Communicate the results of the monitoring of the firm's quality control system process to relevant firm personnel at least annually.
3. **Evaluation of quality control system**
    - Appropriate firm management personnel are then to consider the findings. They should also determine any actions that may be necessary, including any modifications required to the quality control system, and see that these are implemented on a timely basis;
    - Assess:
        - The appropriateness of the firm's guidance materials and any practice aids;

  - New developments in professional standards and regulatory and legal requirements and how they are reflected in the firm's policies and procedures;
  - Compliance with policies and procedures on independence;
  - The effectiveness of continuing professional development, including training;
  - Decisions related to acceptance and continuance of client relationships and specific engagements; and
  - Staff's understanding of the quality control policies and procedures and their implementation.

4. Appropriate complaints handling

The firm is to establish policies and procedures designed to provide it with reasonable assurance that it deals appropriately with:

- Complaints and allegations that the work performed by the firm fails to comply with professional standards and regulatory and legal requirements; and
- Allegations of noncompliance with the firm's system of quality control.

Complaints and allegations, which do not include those that are clearly frivolous, may originate from within or outside of the firm. Staff, clients or other third parties may make complaints or allegations.

As part of this process, the firm is to establish clearly defined channels for staff to raise any concerns, in a manner that enables them to come forward without fear of reprisals.

The firm is then to ensure documentation of the complaints and allegations and the responses to them, including:

- Complaints and allegations that the work performed by the firm fails to comply with professional standards and regulatory and legal requirements;
- Allegations of noncompliance with the firm's system of quality control; and,
- Deficiencies in the design or operation of the firm's quality control policies and procedures, or noncompliance with the firm's system of quality control by staff.

5. Documentation

The firm is to establish policies and procedures requiring appropriate documentation to provide evidence of the operation of each element in its system of quality control.

The form and content of such documentation is a matter of judgment and depends on a number of factors, including the following examples:

- The size of the firm and the number of offices; and
- The nature and complexity of the firm's practice and organization.

The firm is to retain this documentation for a period of time sufficient to permit those performing monitoring procedures to evaluate the firm's compliance with its system of quality control, or for a longer period if required by law or regulation.

7.6 Business Continuity Planning and Disaster Recovery

The key to business continuity planning and disaster recovery is to look at it as an entire function, as whole and complete in itself. The most effective way to coordinate your thinking and planning in this area is to document the various components required in one central document. This is called the Business Continuity Plan.

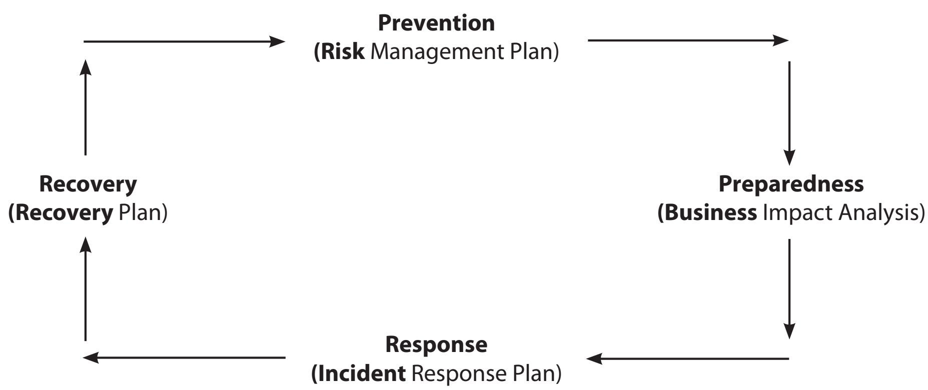
The purpose of developing a Business Continuity Plan is to ensure the continuation of your firm during and following any critical incident that results in disruption to the normal operational capability of the firm.

This section will assist you to prepare a Risk Management Plan and Business Impact Analysis, and create Incident Response and Recovery Plans for your business.

1. Developing a Business Continuity Plan

The Business Continuity Plan is based on the Prevention, Preparedness, Response and Recovery (PPRR) framework. Each of the four key elements is represented by a part in the Business Continuity Planning Process as illustrated in Figure 7.2.

Figure 7.2 Business continuity planning process



It is important that you also consider any legislative or professional accounting body requirement in regard to business continuity or succession planning requirements that are designed to protect the interest of your clients.

2. Prevention

Prevention is all about risk management planning. This is where the likelihood and/or effects of risk associated with an incident are identified and managed. The key elements of the risk management processes are implemented at this stage, with threats identified and dealt with, or reduced to an acceptable level. These have been covered in detail in Section 7.3 of this module, but will be discussed briefly again here to maintain the context of the discussion in this section.

3. Preparedness

The key tool for the Preparedness element is the Business Impact Analysis. This is where the key activities of the firm that may be adversely affected by any disruptions are identified and prioritized.

4. Response

The key function of the Response element is Incident Response Planning. This plan outlines the immediate actions to be taken to respond to an incident in terms of containment, control and minimizing of impacts.

5. Recovery

The Recovery section focuses on recovery planning. The purpose is to outline the actions that are to be taken to recover from an incident in order to minimize disruption and recovery times.

Another important element of the Business Continuity Plan is the concept of regular updates and review. It is hoped that you will never need to use the plan, but if the need ever arises, you should know the plan is up to date with current details, information and resources. This is important, as it should reflect the changing needs of your firm.

The templates and checklists provided in the following sections should be used as a guide only to assist you in developing your own Business Continuity Plan. You should customize it to suit the specific requirements and needs of your firm.

6. **Key items the plan should include:**
   - Distribution list: An up-to-date list should be maintained of the people you have supplied with a copy of the plan and their contact details. Remember to keep a copy of the plan in a safe off-site location.
   - References and related documents: Make a list of all the documents that have a bearing on your Business Continuity Plan.
   - Table of contents: A table of contents should be included at the beginning of the plan.
   - Objectives of the plan: Objectives clarify the purpose of the plan and should describe the intended result. An example of some objectives for a practice would include:
7. **The objectives of this plan are to:**
   - Undertake a risk management assessment of our firm;
   - Define and prioritize our critical practice functions;
   - Detail our immediate response to a critical incident;
   - Detail strategies and actions to be taken to enable our firm to continue operating; and
   - Review and update this plan on a regular basis.

7.6.1 Prevention—Risk Management Plan

You need to manage the risks to your firm by identifying and analyzing the things that may have an adverse effect on it and choosing the best method of dealing with each of them.

There are a number of steps to take in establishing your Risk Management Plan:

1. Select someone to take responsibility for risk management. Typically this will be the practitioner when first establishing the Risk Management Plan. Once established, the management and maintenance of the plan can be delegated to another responsible staff member.
2. Identify the risks. Review the checklists provided in Table 7.2 and Appendix 7.6 as a starting point, and brainstorm with your staff other areas of risk within your firm.
3. Evaluate and prioritize risks. Use the assessment guide provided in Section 7.3 (Table 7.5) as the key tool for this task.
4. Identify possible preventive actions and/or ways in which to minimize the risks.
5. Identify the contingency plans you will establish if the identified threat were to eventuate. You may wish to use a risk assessment table (see Table 7.8).

Table 7.8 Risk assessment table

Key: VH: Very High H: High M: Moderate L: Low					**Date**____________
Risk Description	Likelihood	Impact	Priority	Preventative Action	Contingency Plans
Interruption to process for producing financial statements	L	H	H	Backup copy of data maintained at all times Laptop computers to have current software loaded Cloud-based systems to be reviewed	Off-site storage of all computer programs and client data Cloud-based systems to be reviewed
Client does not pay their account	M	M	M	Regular follow-up with debtors and review of aged listing	Debt collection processes and contact details in place

The questions to ask yourself and your team are:

- What could go wrong?
- What could cause an impact?
- How serious would that impact be?
- What is the likelihood of this occurring?
- Can it be reduced or eliminated?

7.6.2 Preparedness—Business Impact Analysis

The key tool for the Preparedness element is the Business Impact Analysis. This is where key activities of the firm that may be adversely affected by any disruptions are identified and prioritized.

1. Business Impact Analysis

Practitioners should undertake a Business Impact Analysis as part of the firm's Business Continuity Plan. To prepare this, you use the information in your Risk Management Plan to assess the identified risks and impacts relating to the firm's critical activities and determine the basic recovery requirements.

Critical activities are those primary business functions that must continue in order to support your firm. You need to identify:

- Your firm's critical activities;
- The impact on your firm in the event of a disruption; and
- How long your firm could survive if it did not perform this activity.

As part of your Business Impact Analysis, you should assign Recovery Time Objectives (RTO) to each function. The RTO is the time from which you declare that a crisis has occurred to the time that the critical business function must be fully operational in order to avoid serious financial loss.

The following questions will help you and your team determine these critical activities for your firm (see Table 7.9 below):

Table 7.9 Critical activities checklist

No.	Question	Comment/(Example)
1.	List the activities which must be performed to ensure your firm continues to operate effectively: 1. 2. 3. 4. 5.	 Financial statements production
2.	For each activity listed above, complete the following: Activity Name: Activity Description:	 Financial statements production Preparation of financial statements
3.	What is the loss to the firm if this activity could not be provided? Loss of revenue: Increased costs: Staffing impact: Service delivery: Fines or penalties due to missed deadlines: Legal liability, public harm, personal damage: Loss of goodwill, public image: Comments:	 $10,000 per week N/A Staff will need to be reduced No financial statements can be prepared until production resumes Possible/minimal Unlikely Will occur if unable to meet client deadlines Current work in progress of 3 weeks work
4.	What is the maximum amount of time this activity could be unavailable (either 100% or partial) before the losses would occur? Hours: ____________ Days: _____________ Weeks: ____________ Months: ___________ Comments:	 Hours: _________________ Days: __________________ Weeks: 2–3 _________ Months: ________________ If financial statements are not produced within 2–3 weeks, the firm is likely to come under significant pressure from clients, with potential loss of revenue and also losses of clients.

No.	Question	Comment/(Example)
5.	Does this activity rely on any outside or third-party service for its successful completion? No: Yes: If yes, select: Sole supplier: Major supplier: Many alternate suppliers:	 No, all production is done in-house.
6.	On a scale of 1 to 5 (1 being Most Important), where would this activity fall in terms of being important to the operation of the firm 1. 2. 3. 4. 5. Comments:	 1. MOST IMPORTANT!! CRITICAL!! 2. 3. 4. 5. Preparation of financial statements is the primary activity of the firm. The firm is therefore dependent on this activity.
7.	Completed by: ________________________ Name ______________ Date	

Completion of the above questionnaire will allow you to complete the Business Impact Analysis. A suggested Business Impact Analysis is shown in Table 7.10, using the example data shown above.

Table 7.10 Business impact analysis

Critical Practice Activity	Description	Priority	Impact of Loss	RTO (Critical Period before Losses Occur)
Financial statement production	Preparation of financial statements for clients	High	Billings reduced by up to $10,000 per week Some staff may need to be laid off No financial statements can be prepared until production resumes Possible fines due to late lodgment with regulators Likely loss to goodwill if unable to meet client deadlines The firm is likely to come under significant pressure from clients, with potential loss of revenue and also losses of clients if financial statements are not produced within 2–3 weeks	2–3 weeks

7.6.3 Response—Incident Response Planning

The key function of the Response element is Incident Response Planning. This plan outlines the immediate actions that are to be taken in response to an incident in terms of containment, control and minimizing impacts.

7.6.3a Incident Response Plan

The purpose of the Incident Response Plan is to prepare your firm for a timely response to major or critical incidents and reduce the impact of those incidents on your practice operations as identified in your risk assessment. It also prepares key personnel to provide and coordinate an effective response to ensure minimal disruption to the firm's operations in the event of emergency.

Table 7.11 below provides an example of the type of information, including checklists, you might include when planning your response to a major or critical incident. Together these form your Incident Response Plan.

Table 7.11 Incident response checklist

Incident Response	Check X	Actions Taken
Have you: • Assessed the severity of the incident?	☐	
• Evacuated the site if necessary?	☐	
• Accounted for everyone?	☐	
• Identified any injuries to persons?	☐	
• Contacted Emergency Services?	☐	
• Implemented your Incident Response Plan?	☐	
• Started an event log?	☐	
• Activated staff members and resources?	☐	
• Appointed a spokesperson?	☐	
• Gained more information as a priority?	☐	
• Briefed team members on the incident?	☐	
• Allocated specific roles and responsibilities?	☐	
• Identified any damage?	☐	
• Identified critical activities that have been disrupted?	☐	
• Contacted key stakeholders?	☐	
• Understood and complied with any regulatory or compliance requirements?	☐	
• Initiated media/public relations response?	☐	

7.6.3b Evacuation Procedures

You need to have appropriate evacuation procedures that cater to both staff and visitors. These procedures should be stored in a place accessible to all staff.

The objective of an evacuation plan is to provide a set of procedures to be used by site occupants in the event of a critical incident. You should:

- Start with a floor plan of the site;
- Clearly identify the location of emergency exits;
- Develop strategies for providing assistance to persons with disabilities;
- Make sure that everyone knows what to do if evacuation is necessary;
- Select and indicate a meeting place away from the site; and
- Test the plan on a regular basis.

7.6.3c Emergency Pack

If there is damage to the building, or if it must be evacuated and operations need to be moved to an alternative location, the emergency pack can be taken quickly and easily carried off-site or, alternatively, stored safely and securely off-site. Document within your plan what is contained within your emergency pack and when it was last checked.

Items that you may wish to include are:

1. **Documents**

   - Business Continuity Plan—your plan to recover your firm in the event of a critical incident.
   - List of employees with contact details, including home and mobile numbers and even email addresses. You may also wish to include next-of-kin contact details.
   - Lists of customer and supplier details.
   - Contact details for emergency services.
   - Contact details for utility companies.
   - Building site plan (this could help in a salvage effort), including location of gas, electricity and water shut-off points.
   - Evacuation plan.
   - Latest stock and equipment inventory.
   - Insurance company details.
   - Financial and banking information.
   - Engineering plans and drawings.
   - Local authority contact details.
   - Headed stationery and company seals and documents.

2. **Equipment**

   - Computer backup tapes/disks/USB memory sticks or flash drives.
   - Spare keys/security codes.
   - Torch/flashlight and spare batteries.
   - Hazard and cordon tape.
   - Message pads.
   - Marker pens (for temporary signs).
   - General stationery (pens, paper, etc.).
   - Mobile telephone with credit available, plus charger.
   - Dust and toxic-fume masks.
   - Disposable camera (useful for recording evidence in an insurance claim).

3. Notes

- Make sure this pack is stored safely and securely on-site or off-site (in another location).
- Ensure items in the pack are checked regularly, kept up-to-date, and function.
- Remember that cash/credit cards may be needed for emergency expenditure.

This list is not exhaustive, and you should customize it to suit your own firm's situation.

7.6.3d Roles and Responsibilities

Table 7.12 allows you to assign responsibility for completion of each task to one of your designated roles. You will then assign each role, or multiple roles, to one or more staff members and assign backup staff as appropriate.

The staff members involved should then be given this table in order to understand their roles and as a task assignment list for completion of pre-emergency planning and emergency tasks.

You should customize this table to suit your firm's needs and structure.

Table 7.12 Roles and responsibilities list

<table>
<tr><th>Role</th><th>Designated Staff Member</th><th>Alternate</th></tr>
<tr><td>Team Leader</td><td>Name: Brenton Peters
Contact Details:
123-456-7890</td><td>Name: John Johnston
Contact Details:
234-567-8901</td></tr>
<tr><td colspan="3">Emergency responsibilities:
• Ensure the Business Continuity Plan has been activated
• Oversee smooth implementation of the response and recovery section of the plan
• Determine the need for, and activate the use of, an alternate operation site and other continuity tasks
• Communicate with key stakeholders as needed
• Provide important information to the Communication Officer for distribution
• Keep staff apprised of any changes to situation.</td></tr>
</table>

<table>
<tr><th>Role</th><th>Designated Staff Member</th><th>Alternate</th></tr>
<tr><td>Title</td><td>Name:
Contact Details:</td><td>Name:
Contact Details:</td></tr>
<tr><td colspan="3">Emergency responsibilities:</td></tr>
</table>

<table>
<tr><th>Role</th><th>Designated Staff Member</th><th>Alternate</th></tr>
<tr><td>Title</td><td>Name:
Contact Details:</td><td>Name:
Contact Details:</td></tr>
<tr><td colspan="3">Emergency responsibilities:</td></tr>
</table>

7.6.3e Key Contact Sheet

1. Contact list—internal

Use Table 7.13 to document your staff emergency contact details.

Table 7.13 Staff emergency contact details

Person	Contact Number	Email	Responsibilities
Brenton Peters	123-456-7890	brenton.peters@accounts.com	Team leader
John Johnston	234-567-8901	john.johnston@accounts.com	Alternate team leader

2. Contact list—external

Use Table 7.14 to document your external services (including Emergency Services) contact details.

Table 7.14 External services contact details

Key Contacts	Contact Number/s
Police	
Emergency Services	
Ambulance	
Medical	
Security	
Insurance company	
Suppliers	
Water and sewerage	
Gas	
Electricity	
Telephone	
Professional associations	
Computer hardware/software suppliers	
Bank manager	
Landlord	

3. Event log

Use the Event log (see Table 7.15 below) to record information, decisions and actions in the period immediately following the critical event or incident.

Table 7.15 Event log

Date	Time	Information/Decisions/Actions	Initials
DD/MM/YY	Time	Activate Business Continuity Plan	BP

7.6.4 Recovery

This section focuses on recovery planning. The purpose is to outline the actions to be taken to recover from an incident in order to minimize disruption and recovery times. Recovery is the return to your pre-emergency condition. Performing your critical activities as soon as possible after a critical incident is your primary focus.

You will see below the structure for the Recovery Plan (Table 7.16). You should complete this table with the intention of supporting recovery in "worst case" scenarios. It can then be modified according to the degree of loss to your firm. The recovery process includes:

- Developing strategies to recover your firm's activities in the quickest possible time;
- Identifying resources required to recover your operations;
- Documenting your previously identified RTOs; and
- Listing the people who have responsibility for each task and the expected completion date.

Table 7.16 Recovery plan

Critical Business Activities	Preventative/Recovery Actions	Resource Requirements/ Outcomes	Recovery Time Objective	Responsibility	Completed
Production services—halted	Reassess financial position of firm including cash flows due to loss of revenue to meet minimal overheads Minimize overheads, review expenses, and develop plan of action to reduce fixed overheads; include reduction of casual and permanent staff hours Source alternative temporary equipment to continue production Diversify service range of offerings to clients	Put aside cash reserves to cover costs Reduce costs where possible Research new service offerings Identify alternative equipment providers	2 weeks	Practitioner	DD/MM/YY

7.6.4a Incident Recovery Checklist

This checklist (Table 7.17) should be used once the crisis is over and you are looking to re-establish your firm back to full operation. You will need to customize this list to include information specific to your firm.

Table 7.17 Incident recovery checklist

Incident Response	Check X	Actions Taken
Now that the crisis is over, have you: Refocused efforts toward recovery?	☐	
Continued to gather information about the situation as it affects you?	☐	
Assessed your current financial position?	☐	
Contacted your insurance broker/company?	☐	
Developed financial goals and time frames for recovery?	☐	
Kept staff and other key stakeholders informed?	☐	
Identified information requirements and sourced the information?	☐	
Set priorities and recovery options?	☐	
Updated the Recovery Plan?	☐	
Documented lessons learned from your individual, team and firm recovery?	☐	
What is the current financial position of your business?	☐	
Have you determined how much cash your business has currently available by creating a cash flow statement?	☐	
Have you considered and noted your recovery objectives, actions and priorities?	☐	
Have you established a recovery team with clear responsibilities from the recovery plan?	☐	
Can you support such team members working off-site?	☐	
Do you have adequate resources (staff, finances, etc.) to bring the business up to former operating levels?	☐	
Have you priced out your Recovery Plan, and can you afford it?	☐	
Do you have a marketing strategy to promote that you are open for business?	☐	
Have you completed cash flow and profit and loss forecasts?	☐	

Do you intend to fund the reopening of your firm from the firm itself or from other sources?	☐	
Where the business has existing debt financing arrangements, have these been reviewed to ensure that the finance facility and structure fit the new needs of the firm?	☐	
What existing lines of credit does the firm have access to, and can these lines of credit be accessed to fund the reopening of the firm	☐	
Given the potential changed market conditions, are your firm's premises situated in the right location?	☐	
Are there any plans by local government or others that may impact the viability of the location of your firm, such as changes that may restrict access?	☐	
Is the size of your premises too large or too small, given the future potential of your firm?	☐	
Do you still have the plant and equipment your firm needs to restart?	☐	

7.6.4b Update, Maintain and Review

It is critical that you rehearse your plan to ensure that it remains relevant and useful. This may be done as part of a training exercise and is a key factor in the successful implementation of the plan during an emergency.

You must also ensure that you regularly review and update your plan to maintain accuracy and reflect any changes inside or outside the firm.

The following points may help:

- A training schedule must be prepared for all people who may be involved in an emergency at the site.
- Pay attention to staff changes. Incorporate an overview of the plan in new staff induction procedures.
- It is best to use staff titles rather than names.
- If you change your firm's structure or suppliers and contractors, this must be amended in your plan.
- After an event, it is important to review the performance of the plan, highlighting what was handled well and what could be improved upon next time.

Record details of your plan reviews in Table 7.18 below.

Table 7.18 Review of recovery plan

Update/Review Date	Reason for Review	Changes Made

7.6.5 Death or Incapacity of Practitioner

Another key area of risk for the firm is the death or incapacity of the practitioner. Much of what has been discussed in this section so far has concentrated on the risk management processes for the firm itself. However, it is also appropriate to give some attention to risk mitigation strategies for the death or incapacity of the practitioner.

7.6.5a Risk Mitigation Strategies

Risk mitigation strategies to prepare in case of death or incapacitation of practitioner or partners (see Table 7.19 below for a checklist):

1. Document sensitive information

(a) It is important for the practitioner to document and keep in a safe place critical information that is necessary for the effective running and operation of the firm. This information may include:

(i) Client agreements and arrangements;

(ii) Employee agreements and arrangements;

(iii) Supplier agreements and arrangements;

(iv) Personal guarantees provided and to whom;

(v) Bank and finance arrangements;

(vi) Lawyer's name and contact details;

(vii) Intellectual property residing within or developed by the firm; and

(viii) Recommendations for ongoing management of the firm.

2. Maintain adequate insurance

(a) It is important to maintain adequate insurance to cover the practitioner and also the firm.

(b) If the practitioner has partners, it is prudent to ensure that the firm has adequate insurance to cover each partner and to provide the funds to pay out the estate for the partner's share of the firm in the event of their death.

(c) The prudent practitioner will insure their key human assets just as they do their physical assets.

(d) Important insurance coverage to hold includes:

- "Key person" insurance;
- Partnership/shareholder insurance (this provides for payment to the survivors of the partner); and
- Business equity insurance (it is important that the business equity insurance policy is supported by a "buy/sell agreement," as discussed below).

3. Ensure there is a valid "buy/sell agreement"

(a) If there are partners in the firm, it is important to ensure there is a valid "buy/sell agreement." This outlines the terms and conditions agreed upon between the partners for the purchase or sale of their share in the firm.

- Ensure legally drawn buy/sell agreement has been prepared; and
- Confirm it has been reconciled with the partnership/shareholder coverage to ensure there is no shortfall.

4. Inform bankers and suppliers

(a) It is important to consider beforehand what might be the reaction of bankers, other lenders and suppliers to the death or incapacitation of the practitioner.

- Would they be prepared to continue with their financial arrangements, or would they call up their debt?
- Does the business have sufficient financial reserves to cover this situation?

5. Ensure adequate training of staff

(a) Appropriate training should be provided to staff in the key areas of management and the operation of the firm so that it is not totally dependent on the practitioner.

6. Ensure procedures manual written and maintained

(a) It is vital to the ongoing operation of the firm that a procedures manual has been prepared which fully documents the procedures, processes and operations of the practice.

(b) This means the firm is able to continue to operate during the death or incapacitation of the practitioner until certainty as to its future is known.

(c) The procedures manual also becomes a key document in any valuation process which is undertaken, as it tends to add value to the firm by reducing reliance on the practitioner.

7. Ensure job descriptions are completed

(a) It is important that job descriptions have been completed for all roles within the firm and that each staff member is clear on the tasks they are to perform.

8. Undertake regular staff appraisals

(a) Regular staff appraisals allow staff to stay informed of their progress and development within the firm and also provides the practitioner with the opportunity to provide feedback on their performance.

(b) It also provides the practitioner the opportunity to advise the staff member of the steps that should be taken if the practitioner were to die or become incapacitated.

9. Partnership issues

(a) If there are partners within the firm, it is important they clarify what will happen in the event of either their death or their incapacitation.

10. Other business relationships

(a) It is important to understand whether the untimely death or incapacitation of the practitioner or partner would unduly affect any other business relationship that the firm has.

Table 7.19 Checklist of risk mitigation strategies

	Risk	Questions to Ask
1.	Document sensitive firm information	Is the following information documented and in safe keeping: 1. Client's agreements and arrangements; 2. Employees' agreements and arrangements; 3. Suppliers' agreements and arrangements; 4. Personal guarantees provided and to whom; 5. Bank and finance arrangements; 6. Lawyer's name and contact details; 7. Intellectual property residing within or developed by the firm; 8. Recommendations for ongoing management of the firm.
2.	Maintain adequate insurance	Is the following insurance held: 1. Key man insurance? 2. Partnership/shareholder insurance? 3. Business equity insurance?
3.	"Buy/sell agreement"	1. Has a legally drawn buy/sell agreement been prepared? 2. Has this been reconciled with the partnership/shareholder insurance?
4.	Bankers and suppliers	1. Are they prepared to continue with their financial arrangements or would they call up their debt? 2. Does the firm have sufficient financial reserves to cover this situation?
5.	Staff training	1. Have staff been trained in management and the operation of the firm?
6.	Procedures manual	1. Has a Procedures Manual been prepared? 2. Is it maintained and kept current?
7.	Job descriptions	1. Have job descriptions been prepared?
8.	Staff appraisals	1. Are regular staff appraisals held? 2. What is their format?
9.	Partnership issues	1. If there are partners within the firm, have they clarified what will happen in the event either of their death or their incapacitation?
10.	Other business relationships	1. Would the death or incapacitation of the practitioner unduly affect any other business relationship the firm has? 2. Are documented succession planning or continuity plans in place?

7.7 Liability and Insurance within Your Firm

This module has focused on the topic of risk management and discussed strategies to manage or mitigate that risk. You can eliminate some of these risks; however, many risks you have to manage and, over time, try to reduce.

Practitioners in public practice should consider insurance as an important component of their overall risk management strategy. In the process of managing their business risks, practitioners will identify certain risk exposures that could have a significant impact on their firm. As discussed throughout this module, the approach to take is to identify the risk, quantify the risk, and treat the risk.

However, when you reach the conclusion that a risk is too great to hold, the option is to transfer the risk. Insurance is one of the oldest forms of risk transfer, and professional indemnity insurance is a mandatory requirement for members of some professional bodies and regulators.

For the practitioner, there are many different types of insurance that can provide protection now and in the future. It is important to choose the most appropriate form of insurance to suit your circumstances. To do this, you will need to understand your position and the level of exposure and liability you may be facing.

For most types of insurance coverage, an insurance broker will act as your representative. The broker will approach the underwriting market on your behalf. Accordingly, it is important to have confidence in your broker's ability to know your profession, understand your risk profile and convey it correctly to the underwriters. It is also important that your insurance broker meets the appropriate licensing requirements for your geographical location.

Your broker should have not only a good understanding of your profession but also a solid grounding in insurance law. It is useful for you to understand the underwriter and qualitative policy issues, such as their experience in the profession and how suitable the coverage is. It is important to determine whether the underwriter is prepared to provide assistance to reduce your risk.

7.7.1 Professional Indemnity Insurance

Professional indemnity protects a practitioner against their legal liability toward third parties for injury, loss or damage arising from their professional negligence or that of their employees.

Levels of coverage can vary greatly from insurer to insurer. Among the issues you need to consider are the extent of the coverage, applicable excess, retroactive date, geographical coverage and exclusions. You should also be clear on what is included in the insurance coverage you are taking on.

7.7.1a Coverage for all of Your Work

You must be fully informed of any restrictions, limitations or exclusions on policies that can affect the coverage you have for your activities. Where possible, you should obtain written confirmation of the coverage provided for the areas of work you are doing. Examples of these activities, subject to jurisdictional regulations, include:

- Audit work;
- Investment advice;
- Pension planning;
- Eldercare services;
- Mortgage/finance broking;
- Insolvency;

- Mergers and acquisitions;
- Buying or selling businesses;
- Migration;
- Work for deceased estates; and
- Insurance and risk management advice.

7.7.1b Other Issues to Consider

1. Identifying your risks

It is important to fully disclose all the facts concerning your risk profile when you apply for professional indemnity insurance coverage. The proposal form plays a critical role in helping the insurer understand this.

The majority of professional indemnity insurances are not renewable contracts, which means the policy will terminate on the expiration date. Accordingly, you will need to submit a new proposal form for coverage before the current policy expires. The information you provide in the proposal gives the underwriter the information they need for their quote and the basis for their position.

2. Reinstatements of the limit of indemnity

Unlike other forms of liability policy, the sum insured by the professional indemnity policy typically is limited, so that the limit applies to the aggregate of all claims against the policy during the policy period. An automatic reinstatement allows this aggregate limit to be increased for the number of reinstatements specified in the policy, while the limit for any one claim remains the limit of the sum insured. As this may vary from policy to policy, it is preferable to have unlimited reinstatement of the limit of indemnity.

3. Retroactive date

The retroactive date is the date after which acts, errors or omissions of the insured are covered. Any act, error or omission arising from work done after the retroactive date will be covered under the policy. The inception date is the start of the policy period.

Any limitation on your retroactive coverage could affect coverage for some or all of the work you may have done in the past. Carefully consider the impact of any such limitation.

4. Coverage for past firms or business

Check whether your policy covers you for claims made in connection with a previous firm or other business.

5. Extensions to standard coverage

Extensions likely to be available include:

- Libel and slander;
- Loss of documents;
- Dishonesty;
- Fidelity;
- Outgoing and/or incoming partners; and
- Inquiry costs and complaints resolution services.

Some of these extensions may be automatic if the policy provides coverage for any civil liability. It may be worthwhile checking to see if any other extensions are offered.

6. Run-off coverage

Run-off is a term used by the insurance industry to describe how a firm will reduce (or “run-off”) its liability to its clients after it has ceased operating. It is simply a professional indemnity policy that provides limited coverage (that is, coverage limited to work done prior to the date the firm closed).

Professional indemnity insurance is underwritten on a “claims made” basis. A firm is therefore only covered against claims that may be made against it for work it performed while operating, for as long as that firm maintains insurance protection.

Run-off coverage can only be provided to a firm that is no longer operating. Such a firm may be closed because the partner(s) has retired or following the sale of the business to another firm.

There is no limitation on your liability to your clients and therefore no limitation on the period of time for which the insurance needs to be continued. Coverage simply needs to be continued until the firm’s partners feel satisfied that there is no longer any likelihood of problems with their work.

7.7.2 Other Types of Insurance to Consider

The following types of insurance may be worth considering for your firm. However, be aware that different insurances and requirements may apply in your local jurisdiction. This information is provided for guidance purposes only.

1. Business interruption or loss of profit insurance

This type of insurance covers the firm for interruption due to damage to property by fire or other insured perils. The coverage should ensure that ongoing expenses are met and that anticipated net profit is maintained through a provision of cash flow.

2. Building and contents insurance

This insurance should cover the building premises and contents of the firm, as well as contents and stock, against loss due to a number of circumstances.

3. Public liability insurance

Public liability insurance should cover the owner and business against the financial risk of being found liable to a third party for death or injury, loss or damage of property, or economic loss resulting from the firm or practitioner’s negligence.

4. Key person insurance

This type of insurance should help cover the loss of a key member of staff.

5. Personal accident and illness insurance

This insurance is important for practitioners to cover their own positions as self-employed operators, subject to local and jurisdictional requirements.

6. Burglary and theft coverage

Firm and business assets should be protected against burglary by this type of insurance. This may also be covered under property contents insurance.

7. Fidelity guarantee

Losses resulting from misappropriation by employees who embezzle or steal should be covered by this insurance.

8. Plant and equipment/machinery breakdown insurance

This insurance should protect the firm against plant and equipment and machinery breakdown—this is important where there is high dependence on computer hardware. These items may also be covered under property contents insurance, but it is worth checking the specific policy.

7.8 Conclusion

This module has discussed the issue of risk management and the specific impact it has on accounting firm life. It has provided a framework for identifying, evaluating and acting on risks you identified within your firm.

It also discussed the ethical issues you must be aware of in a firm and discussed the safeguards that can be put in place to help you deal with ethics threats. The module went on to discuss quality control processes and the important role they can play in managing the firm's risks. It then covered business continuity planning and included strategies on how to deal with the death or incapacity of the practitioner.

The module finished with a discussion on liability and insurance within your firm and reviewed the types of insurance likely to be most relevant to the practitioner. Practitioners are encouraged to be watchful and remain vigilant for all areas of risk within their firm and look for ways to reduce or eliminate those areas where their risk is at an unacceptable level.

7.9 Further Reading and IFAC Resources

The IFAC Global Knowledge Gateway is a digital hub where professional accountants can easily access thought leadership and resources from IFAC, member organizations, and other notable groups and individuals.

The Gateway Practice Management section includes additional articles, videos, and resources to complement this module. We encourage you to review the content, provide feedback, engage with contributors, and share your own insights on contemporary practice issues.

Appendix 7.1 Leadership Responsibilities for Quality Control within a Firm

ISQC 1 Paragraphs 18 and 19

In compliance with ISQC 1, the firm recognizes the importance of promoting an internal culture that recognizes quality control as essential in performing engagements. Ultimate responsibility for the firm's system of quality control has been accepted by the partner(s)/principal/managing board of partners, and as such the firm has established policies and procedures which address each of the elements of a system of quality control as described in ISQC 1.

Partner(s)/principal/managing board of directors assigns operational responsibility for the firm's system of quality control to:

(insert name/s) ____

who has/have sufficient and appropriate experience and ability, and the necessary authority, to assume that responsibility, and who has/have accepted the role.

Signed ____________________

Date ______________________

Signed ____________________

Partner ____________________

Date ______________________

Appendix 7.2 Circumstances and Relationships Requiring Notification (to Engagement Partners in the Case of Assurance Engagements)

Where an employee (or assurance team member) is aware of a relationship/association with a client, a quality-control officer needs to be notified so that appropriate action can be taken. Such relationships/ associations include:

- Employment of family or friends by the client;
- Future or recent employment with client serving as officer, director or company secretary of client;
- Close business relationship with client;
- Financial interest in the client;
- Having loans and or guarantees to or from the client;
- Receiving a gift, benefit or hospitality from the client; and
- Any other association that may compromise integrity and objectivity.

Upon notification, engagement partner/partner responsible for evaluating any threats to independence and objectivity will take appropriate action to eliminate those threats or reduce them to an acceptable level by applying safeguards. Documentation provides evidence of how threats that have been identified have been dealt with. Below is a pro forma template for assurance practices from the IFAC *Guide to Quality Control for Small- and Medium-Sized Practices.*

Schedule A
Partner and Staff Independence

List and briefly explain the nature of all matters that to the best of your knowledge and belief might affect independence. Refer to Parts 4A and 4B of the IESBA Code when completing the list.

Each item will be reviewed by the engagement partner. Further information may be necessary to determine what action, if any, is required.

All decisions and the course of action to be followed shall be fully documented.

Description	Detail how Independence Might be Affected	Appropriate Safeguard Applied (if Applicable) and/ or other action taken to Eliminate or Reduce Threats to an Acceptable Level

Appendix 7.3 Annual Independence Confirmation

Instructions

All team members, including partners, should complete this form to assess their compliance with the firm's independence policies and procedures. It should be completed:

- By new employees as part of the orientation process;
- At each annual employee performance review; and
- By partners annually.

Name of employee ……………………………………………………………………………

Yes	**No**	
☐	☐	Do you have a direct or indirect material financial interest in a client or its subsidiaries/affiliates?
☐	☐	Do you have a financial interest in any major competitors, investors in or affiliates of a client?
☐	☐	Do you have any outside business relationships with a client or an officer, director or principal shareholder having the objective of financial gain?
☐	☐	Do you owe any client any amount (except as a normal customer, or in respect to a home loan under normal lending conditions)?
☐	☐	Do you have the authority to sign checks for a client?
☐	☐	Are you connected to a client as a promoter, underwriter or voting trustee, director, officer or in any capacity equivalent to a member of management or an employee?
☐	☐	Do you serve as a director, trustee, officer or employee of a client?
☐	☐	Has your spouse or dependent child been employed by a client?
☐	☐	Has anyone in your family been employed in any managerial position by a client?
☐	☐	Are any billings delinquent (high WIP) for clients that are your responsibility?

If you answered YES to any of these questions, you must detail the reason for this threat to independence on the independence resolution memorandum, together with an explanation of how the threat to independence has been eliminated or reduced to an acceptable level.

I have read the independence policy of the firm, and the IESBA's International Code of Ethics for Professional Accountants (including International Independence Standards), and I believe I understand them. I am in compliance except for the matters on the independence resolution memorandum.

Signature of employee ……………………………………………… Date ………………..

Signature of partner…...……………………………………………… Date ………………..

Appendix 7.4 New Client Acceptance Checklist

Instructions

This form should be used to document the decisions to accept the client.

Warning: Practitioners are reminded that care should be taken when completing this checklist to avoid any possibility of defamation of individuals, for example, in the course of assessing their integrity.

Client …………………………………………………… Date ……………………

	Comments
Client integrity has been considered, and we do not have any information that would lead us to conclude that the client lacks integrity.	
Competent to perform engagement?	
Resources to complete on time?	
Independence considerations: Assurance engagement—independence checklist completed? Non-assurance engagement—no significant threats to independence?	
Fee level/collection issues?	
Consideration of client screening questions?	
Genuine reason for leaving previous accountant?	
Any conflicts of interest considered and threat reduced to an acceptable level?	
Ethical letter response considered?	

Record keeping and accounting system review visit scheduled Y/N

Date ………………………………………

Decision made to accept client Y/N

Review of client information on government registers
and necessary follow-up Y/N

Client engagement task checklist completed Y/N

Engagement letter sent Y/N

Add to team meeting agenda to inform staff Y/N

Prepared by …………………………………………….. Date …………………

Partner review ………………………………………….. Date …………………

Appendix 7.5 Client Engagement Procedures: Changes in Professional Appointments

Client name ………………………………………………………………… Year end ……………..

	Comments	Initials
1. Request prospective client's permission to communicate with the existing auditor. If permission is refused, decline the appointment.		
2. If permission is received, write to the existing auditor requesting all information that ought to be made available to enable the prospective auditor to decide whether or not to accept the appointment. Reasons for not accepting the appointment could include ethical and commercial reasons: outstanding fees owed to the predecessor auditor are not of themselves grounds for declining.		
3. The existing auditor must obtain the client's permission to give information to the prospective auditor. If permission is withheld, the existing auditor should inform the prospective auditor, who should decline the appointment.		
4. Communication received from predecessor auditor (can be verbal or written). Such communication must be treated in the strictest confidence, whether or not the appointment is accepted.		
5. Note any reasons given by the existing auditor as to why the appointment should be declined. The existing auditor is required to give specific reasons to the prospective auditor.		
6. If no reply is received from the existing auditor, send a follow-up request by recorded or registered delivery, stating a deadline after which it will be assumed that there are no professional reasons why the appointment should be declined.		
7. If no reply is received from previous auditor, obtain proof of resignation or valid removal from office.		
8. Type the individual's name and company name into Internet search engine. Investigate any unusual hits or reports of illegal or unethical behavior.		

Appendix 7.6 Risk Management Checklists

Identifying potential risks in a firm

a. Services performed	
☐	Have you adequately scoped the assignment, and in particular excluded areas that you are not accepting responsibility for?
☐	How do you evaluate knowledge/experience requirements for both new and ongoing work?
☐	How do you assess client expectations/intended use of reports?
☐	Is the service provided high risk? (e.g., assurance engagements undertaken or provided)
☐	Can you deliver an objective report, or does the client require subjective judgment?
b. Contract risk	
☐	How do you formally agree on the terms of engagement and any variation?
☐	Do you utilize “standard terms and conditions” for all engagements?
☐	Can your liability be capped?
☐	How do you manage “contingency fees” or performance-based remuneration?
☐	Are you precluded from holding financial interests in the client or receiving commissions?
c. Acceptance/Continuance risk	
☐	How are you formally assessing potential clients for acceptance?
☐	Why is the client changing accountants?
☐	Have any other professionals rejected the potential client?
☐	Are there early signs of disputes on the fees that are proposed to service the client?
☐	Has the client allowed sufficient time for the acceptance process to be completed?
☐	How do you evaluate retention of clients from time to time?
☐	How do you address any conflict of interest?
☐	How are you maintaining independence?
☐	Are there any concerns about a client’s viability, reputation, or management?
d. Performance risk	
☐	Do you seek the opinion of a second partner or an external “mentor”?
☐	How are you maintaining confidentiality?
☐	Are fees too low for quality work?
☐	Are you investing enough in continuing professional development for yourself and your staff?
☐	Have you complied with minimum continuing professional development requirements?

☐	What is the level of your professional indemnity insurance?
☐	Is it adequate in terms of level and policy conditions?
☐	Have you declared all services offered to the underwriter?
☐	Are you aware of the potential of a claim, and have you given notice to the underwriter during the period of insurance or on your proposal for insurance?
☐	Have you a claim for fees that could result in a client counter-claiming for negligence?
☐	What are the risks of the performance of different professionals from within the firm?
☐	Are other professionals covered by liability capping schemes?
☐	How are you engaging subcontractors/agents/consultants, and how are you indemnified in respect to their work?
☐	Have you considered skill levels, levels of insurance coverage, and is there an indemnity in place?
☐	Are you or is your advertising/promotional material deceptive or misleading as to your skill, qualifications, etc.?
☐	How have you given appropriate guidance and assistance to personnel?
☐	How have you given appropriate supervision to personnel?
☐	How have you appraised ongoing performance of personnel?
☐	Do you have appropriate inspection and review processes in place?
☐	Have the roles and responsibilities of personnel relative to risk management been defined and communicated?

Integrity

Questions to consider:

Integrity checklist

No.	Question	Comment	Date Completed
1.	Do you review client files?		
2.	How often do you review each client's files?		
3.	Do you have operational notes in client files (e.g. software, postal preferences, etc.)?		
4.	Do you have criteria for new clients and for client retention? Are they documented?		
5.	Do you use an engagement letter? To whom are they sent and how often?		
6.	Does your firm use checklists? Is there a central list of these? Who uses the checklists in the office? How often are they updated and by whom?		
7.	Do you have documented procedures such as manuals, standard letters, etc.? If so, where are they kept?		
8.	Who in the firm is the person responsible for managing the procedures of quality control to ensure all work is performed to a high quality?		

Services offered

Questions to consider:

Services offered checklist

No.	Question	Comment	Date Completed
1.	Do you know what services your firm offers? Is there a centralized list available for clients and staff?		
2.	Do you offer services that you are not qualified to offer?		
3.	Do you ensure that the services you offer are well known to the clients in the form of an engagement letter?		
4.	Are the staff members allocated to clients' work capable and trained in the relevant area?		
5.	Are the services right for your firm's profile and resources?		
6.	Do you have the resources to meet delivery of the services to be performed?		
7.	Do you have a referral network, and how do you ensure quality control for referral?		
8.	Do you outsource any part of your work, and do you ensure quality control (e.g., bookkeeping, auditing, etc.)?		

Marketing and communication

Questions to consider:

Marketing and communication checklist

No.	Question	Comment	Date Completed
1.	Do you have a marketing and/or strategic plan suitable for your firm (big or small)? If so, how is this monitored and appraised for any risks?		
2.	Is this plan documented and communicated to any or all of your staff? If so, how is this done? If not, why not?		
3.	Every firm has a culture. Have you identified your firm's culture? If so, are your staff aware of it?		
4.	Do your clients understand the culture of the firm, and, if not, do you see the need for communicating it to them?		
5.	Have you considered your competition in your marketing plan?		

Staff and human resources issues

Questions to consider:

Staff and human resources checklist

No.	Question	Comment	Date Completed
1.	Do you have staff, and have you identified each of their roles?		
2.	Do you have employee work contracts or similar for your staff? If not, it is highly recommended that you do provide each staff member with a work contract.		
3.	Have you considered your staff's security and personal safety?		
4.	Do you have an occupational health and safety policy? Is it enforced and practiced?		
5.	Does your firm have a complaint resolution policy?		
6.	Do you have a staff induction procedure?		
7.	How do you monitor staff performance? When is this done, and how often?		
8.	How are staff trained and updated on important office and regulatory changes?		
9.	Are your staff members properly supervised? Is their work reviewed?		
10.	If staff members give advice to clients, are you aware of the advice given? Are they covered under your professional indemnity insurance policy?		
11.	If they give advice, is it monitored and recorded for future reference?		
12.	How do you ensure that you or any of your staff are properly qualified to give the advice to the clients?		

Information and resource management

Questions to consider:

Information and resource management checklist

No.	Question	Comment	Date Completed
1.	Identify/describe any electronic medium you use to communicate with government regulators or any other government body you interact with.		
2.	Identify how you take reasonable care when advising clients and interacting with the various legislative requirements.		
3.	How do you keep up-to-date with all the latest changes that may affect your firm and that of your clients? How do you keep your staff informed?		
4.	What steps do you take to ensure that you are not professionally negligent?		
5.	Where do you obtain your information and resources that you rely on? Are your information sources reliable? Do they support your obligation to take reasonable care?		
6.	Do you know what your obligations are with regard to professionalism?		
7.	Do you and your staff comply with continuing professional development requirements? How do you keep up-to-date? How is this monitored?		

Regulatory obligations

Questions to consider:

Regulatory obligations checklist

No.	Question	Comment	Date Completed
1.	What is your procedure for filing of your firm's forms with all government and regulatory bodies?		
2.	Do you have a client list? Do you know what role you play for each client?		
3.	Do you monitor your client list according to the filing and reporting program?		
4.	In regard to workflow for your firm, do you know what is to be completed and the current status of each job at any given point in time? How do you do this?		
5.	Do you communicate with your clients regarding their filing and reporting obligations, and your work flow?		
6.	Do you measure your filing and reporting performance? How do you do this?		
7.	Do you identify any risks associated with late filing and penalties? Do you communicate with your clients once any risks are identified?		

Information technology and security

Questions to consider:

Information technology and security checklist

No.	Question	Comment	Date Completed
1.	How secure is your hardware, software, and any information that is stored electronically?		
2.	Is all your software licensed? If not, have you considered the risks to your firm?		
3.	How do you guard your firm against pirating/copying of your software?		
4.	Backups: What backup plans do you have in place? Do you know whether your backup restores successfully? Do you test your backups? Who is responsible for this function in your firm? Where is this process documented?		
5.	Internet: What virus protection (if any) do you have? How frequently is this updated? What policies do you have regarding information downloads that are inappropriate? Is this documented? Do you have a firewall? Do you have anti-spam software?		
6.	Emails: Do you have policies and procedures to manage the email use of your staff? Do you have a disclaimer outlining the “limited liability scheme” and the “privacy statement” where applicable?		
7.	Do you have immediate assistance or technical specialists on hand, or easily available, if you suffer computer or software failure?		

Management collapse—succession planning

Questions to consider:

Management collapse—succession planning checklist

No.	Question	Comment	Date Completed
1.	Who is the principal/main partner of the firm? Does the same person have the responsibility for office management? If not, who has that responsibility?		
2.	Is there anyone else in the firm who can manage this responsibility in the event that the primary person becomes unable to?		
3.	What backup arrangements are in place if the principal person is unable to carry on?		
4.	If you are a sole trader, have you considered what possibilities could put you out of action for an extended period of time?		
5.	Do you have any plans for when your staff are sick for extended periods of time?		
6.	Do you have contingency plans for your firm in the case of fire, flood or other disaster?		
7.	Regarding delegation, are there any areas of practice which only one person is familiar with? Consideration should be given to cross-training of staff, so the firm has at least two people who know each particular job.		

Acceptance or continuance of clients

Questions to consider:

Acceptance or continuance of client's checklist

No.	Question	Comment	Date Completed
1.	How often do you review your clients and whether they meet your acceptance criteria?		
2.	Do you evaluate retention of clients from time to time?		
3.	Do you note any client disputes that could potentially lead to a professional indemnity issue? Do you then inform your insurance company?		
4.	Have you ensured that your objectivity and integrity are not jeopardized?		
5.	How are you maintaining client confidentiality?		

Cash flow management

Questions to consider:

Cash flow management checklist

No.	Question	Comment	Date Completed
1.	Do you have a credit management policy? Who is responsible for this in your firm?		
2.	Do you have contingency plans to cover you in a deficit cash flow position?		
3.	Do you have sufficient working capital to sustain your firm, now and in the future?		
4.	Is your business trading in a solvent position?		