

Quality Management at the Engagement Level (ISA 220)¹—Issues and Discussion

Approved minutes of the December 2016 IAASB's discussions on this topic (the last time this topic was discussed with the Board) can be found in the Appendix to this paper.

ISA 220 is premised on the basis that the firm is subject to ISQC 1² or to national requirements that are at least as demanding. Therefore, the work on ISA 220 is closely aligned with the work on ISQC 1. This paper makes extensive reference to the work being done to revise ISQC 1 and incorporates terms and addresses matters currently being contemplated in that revision (including as it relates to the proposal to introduce a quality management approach (QMA) within ISQC 1). Accordingly, this paper should be read after having read, or in combination with reading, Agenda Items 2-A, 2-B and 2-C.

Objectives of the Agenda Item

The objective of the agenda item is to obtain Board views on the matters set out in this paper, together with the proposed changes to extant ISA 220 set out in **Agenda Item 5-B**, in order to help the ISA 220 Task Force³ (the "Task Force") make progress towards developing an exposure draft of revisions to ISA 220.

Background

1. A project proposal⁴ that addressed the revision of the IAASB's quality control standards (ISQC 1 and ISA 220) was approved by the IAASB in December 2016. This project proposal followed outreach and extensive consultation about issues and concerns related to these standards, including:
 - Findings from the IAASB's ISA Implementation Monitoring Project, which was completed in 2013.
 - The IAASB's Invitation to Comment (ITC), [Enhancing Audit Quality: A Focus on Professional Skepticism, Quality Control and Group Audits](#), which set out the issues related to quality control at the firm and engagement level, and group audits (ISA 600),⁵ including highlighting areas of crossover between these standards.

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

² ISQC 1, *Quality Control for Firms that Perform Audits and Reviews of Financial Statements, and Other Assurance Engagements and Related Services Engagements*

³ Formerly the Crossover Task Force.

⁴ http://www.iaasb.org/system/files/meetings/files/20161205-IAASB_Agenda_Item_9A-GA-and-QC-Project-Proposal.pdf

⁵ ISA 600, *Special Considerations—Audits of Group Financial Statements (Including the Work of Component Auditors)*

2. In December 2016, in addition to discussing matters related to finalizing the project proposal, the IAASB also discussed various matters relating to possible changes to ISA 220. In summary, Board members:
 - Supported linking the objective of the auditor to managing quality of the audit, although it was noted that more clarity about how this would be operationalized in ISA 220 was required (in particular, the IAASB noted that the distinction and interaction between a risk assessment for these purposes (i.e., risks to quality) versus the identification and assessment of the risks of material misstatement as required by ISA 315 (Revised)⁶ would need to be clear);
 - Supported clarifying the engagement partner's (EP) overall responsibility and accountability for audit quality at the engagement level, while still allowing the EP to assign certain responsibilities to other members of the engagement team (ET) as necessary and appropriate;
 - Encouraged the Task Force to perform further consideration of situations where the signing partner is different from the EP who was responsible for the direction, supervision, and review of the work performed as a part of the audit;
 - Noted the need for appropriate coordination with the International Ethics Standards Board for Accountants (IESBA) relating to considerations around the definitions of EP, ET, and network firms;
 - Supported a new requirement(s) related to strengthening two-way communication among the members of the ET and those involved in the audit on a timely basis throughout the audit; and
 - Supported further consideration of how firms in networks interact, especially as relates to quality control (see **Agenda Item 4-A** for discussion about matters related to networks).
3. ISQC 1 is being revised to introduce a QMA. The matters currently being presented for discussion with the IAASB include proposals from the Quality Control Task Force (QCTF) regarding possible revisions to ISQC 1, including a revised structure. This proposed structure incorporates: (1) Governance and leadership, including organization, culture and strategy; (2) Information, communication, and documentation; and (3) The quality management process (e.g., establishing quality objectives, performing quality risk assessments, designing and implementing responses to quality risks, and monitoring and remediation)—the proposals of the QCTF are fully explained in **Agenda Items 2-A, 2-B, and 2-C**.
4. As the various Task Forces⁷ working on the revisions of the quality control standards and ISA 600 have progressed their work, the interactions and crossover between the various standards have been confirmed and further highlighted. In particular, it has been identified that many issues involve a coordinated approach to ensure that the issues are dealt with in the appropriate standard(s) and in a consistent and inter-related way. For example, ISQC 1 acknowledges that in designing responses to manage quality at the firm-level, firms may establish requirements for certain activities and procedures that are intended to be performed at the engagement level. The execution of these activities and procedures then become the responsibility of the EP, and are relevant to managing quality at the engagement level. This relationship needs to be built into ISA 220, i.e., ISA 220 needs

⁶ ISA 315 (Revised), *Identifying and Assessing the Risks of Material Misstatement through Understanding the Entity and Its Environment*

⁷ This includes the ISA 220 Task Force, QCTF, and the Group Audits Task Force.

to build off the principles established in ISQC 1 and deal with the issues in the context of what is relevant to managing quality at the engagement level, and the related responsibilities of the EP. In turn, ISA 600 should then build off the principles established in both ISQC 1 and ISA 220, but in the context of an audit of group financial statements where one or more component auditors may be involved.

5. One of the crossover matters related to ISQC 1, ISA 220 and ISA 600 are the various issues and concerns relating to network⁸ structures. This topic is covered separately in **Agenda Item 4-A**.
6. The recommendations of the Task Force included in this agenda item have been developed based on the overall objective of embedding quality management principles and focusing on quality management at the engagement level, and taking into consideration:
 - The changes being proposed for ISQC 1.
 - The inter-relationship between firm-level actions and responses to manage quality, and what is required or expected at the engagement level, i.e., including responses to address certain requirements in ISQC 1 that are established at the firm level, but are nevertheless intended to be implemented at the engagement level and therefore as such, become matters for which the EP is responsible.
7. The Task Force acknowledges that the appropriate approach to managing quality at the engagement level can and will vary from one engagement to the next. The Task Force is of the view that the approach set out below is adaptable to audits of different sizes and complexity. It is premised on, and provides for, professional judgment being the basis for addressing the requirements, in particular those relating to determining the nature, timing and extent of direction, supervision and review by the EP (and other team members), which forms the basis for the conclusion that the EP has been sufficiently involved in the audit.
8. In debating the changes presented below, the Task Force is of the view that such revisions to ISA 220 could be expected to:
 - Enhance decision-making and improve the process of planning an audit engagement;
 - Lead to a more effective allocation and management of resources to an audit engagement by the firm, and within the audit ET;
 - Increase the probability of delivering a high-quality audit engagement;
 - Support the decision-making process by the firm on whether to accept or continue an audit, and drive more informed conclusions being reached;
 - Assist with adapting quality management at the engagement level to a wide variety of circumstances by causing more deliberate consideration of how quality may not be effectively managed for a particular engagement in the context of the elements of ISA 220, and appropriate responses should be developed;

⁸ Our standards define a “network” as “a larger structure that is (a) aimed at cooperation; and (b) is clearly aimed at profit or cost-sharing or shares common ownership, control or management, common quality control policies and procedures, common business strategy, the use of a common brand name, or a significant part of professional resources.” Firms that operate through such arrangements are typically referred to as a network or network firms.

- Reinforce the importance of the EP’s determination of the nature, timing and extent of necessary involvement in the engagement, and provide for the ability of the approach to be applied to a wide variety of circumstances (e.g., that the requirements can be ‘flexed’ as appropriate in situations where there is a small, non-complex entity and when entities are larger or have more complex issues);
- Focus auditors on controls over the use of technology tools being used; and
- Encourage an enhanced understanding of (and response to) factors that may incentivize or dis-incentivize the appropriate application of professional skepticism by the ET.

9. This paper is organized into the following sections:

| | |
|-----------|--|
| Section A | Interaction of ISA 220 with ISQC 1 and Other Relevant ISAs |
| Section B | Quality Management at the Engagement Level |
| Section C | The Overall Responsibility of the Engagement Partner for the Audit |
| Section D | The Core Elements to be Addressed on All Audits |
| Section E | Way Forward |

10. This paper should be read in conjunction with the possible changes to ISA 220 set out in **Agenda Item 5-B**.

A. Interaction of ISA 220 with ISQC 1 and Other Relevant ISAs

11. Extant ISA 220 deals with the specific responsibilities of the auditor regarding quality control procedures for an audit of financial statements. In particular, it sets out requirements dealing with the responsibilities of the EP, and where applicable, the responsibilities of the engagement quality control reviewer. The proposed revisions to ISA 220 (set out in Sections B–D below) have been developed in light of the proposed revisions being made to ISQC 1 and are intended to help the auditor focus on quality management at the engagement level.
12. In order to meet the objectives of ISQC 1, firms establish the foundation for quality management for all engagements undertaken by the firm by identifying and addressing risks to quality, and implementing responses to those risks. The objective of ISA 220 is focused on the management of quality at the engagement level, but this objective needs to be addressed in the context of the firm’s system of quality management as it relates to an audit of financial statements. ISA 220 therefore needs to demonstrate how the principles or requirements established in ISQC 1 are embedded and applied at the engagement level for audit engagements.
13. In developing the changes to ISA 220, the Task Force is of the view that the linkages and inter-relationships between quality management at the firm-level and at the engagement-level need to be strengthened and further clarified. This includes making it clear in ISA 220 that the EP has responsibility for: (i) understanding how the responses that the firm has designed to address risks to quality at the firm level are relevant to the audit engagement for which the EP is responsible; and (ii) for taking appropriate action to effectively implement the responses at the engagement level, or to

determine that they are executed as expected. The proposed changes to ISA 220 for such responsibilities are further discussed in Section C of this paper.

14. To strengthen the link to ISQC 1 for the firm’s system of quality management, the Task Force therefore proposes including additional paragraphs in the introductory material in ISA 220 to highlight that ISA 220 expands on how quality management principles in ISQC 1 are applied for audits of financial statements, and through providing more context about what ISQC 1 requires for firms (see revised paragraph 1, 2, and new paragraphs 2A and 2B, in **Agenda Item 5-B** (also note the proposal to develop additional application guidance)). Furthermore, in the changes that are being proposed to the core elements of ISA 220 (further explained in Section B below), the requirements will focus the auditor on understanding what policies or procedures, or actions, the firm has in place or requires before considering what further response is necessary at the engagement level. The Task Force is of the view that the introductory paragraphs of ISA 220 need to highlight that the firm’s policies or procedures form the foundation of the EP’s responsibilities for managing quality, including setting out the EP’s role and responsibilities in managing quality at the engagement level. These introductory paragraphs will also then support the changes being proposed in relation to what the EP is required to do in relation to each core element that is required to be addressed in managing quality at the engagement-level (described further in Sections B–D of this agenda item).
15. The Task Force has also discussed how to clarify the responsibilities of the EP. The Task Force is seeking to reiterate the fundamental premise that the EP is responsible for managing quality for an audit of financial statements, however the Task Force notes that it is not possible nor practical for the EP to personally perform all the procedures that might be relevant in addressing the requirements of ISA 220. The Task Force also believes that the EP should be sufficiently involved in the engagement in order to have a basis for demonstrating how the EP has addressed the requirements relating to managing quality at the engagement level (e.g., as demonstrated through sufficient and appropriate involvement in the direction, supervision and review of other members of the ET and others involved in the audit). The Task Force has therefore proposed including background material to this effect in the revisions to ISA 220 (see paragraph 3A in **Agenda Item 5-B**). Note that this concept is also addressed further in the proposed revisions to paragraphs 15 and 16 of extant ISA 220 – see Section D related to Engagement Performance. In developing these changes, the Task Force agreed that:
 - It should be made clear that the EP may assign activities to others to assist the EP in fulfilling his or her responsibilities; however being mindful of any specific requirements of the ISAs whereby an EP may have to perform certain procedures and any firm requirements whereby certain policies or procedures are required to be addressed or performed specifically by the EP. The Task Force has considered developing application material that would include guidance, including some examples, about responsibilities that cannot be assigned.
 - In each of the core elements of ISA 220, it should be made clearer what the EP’s responsibilities are. The Task Force is of the view that the changes proposed in section D below, will help EPs to understand more specifically what their responsibilities are.

The Task Force has also considered the need to revisit how terminology is used throughout ISA 220, and whether revisions are needed to drive more consistent understanding and application:

- For example, use the term “engagement partner” where the requirement is addressing something that is the specific responsibility of the EP, and “auditor” where the specific procedure may be assigned to another member of the team or someone else involved in the

audit. The Task Force will further consider this approach as the revision of ISA 220 is progressed, but is preliminarily of the view that it may result in changes that are too subtle and not easily understood. The Task Force also notes that the majority of the requirements in extant ISA 220 are directed at the EP, and does not anticipate changing this in the proposed revisions.

16. The proposed revisions to ISQC 1 also strengthen the requirements in relation to obtaining or generating and communicating between the firm, ETs, personnel performing functions in relation to the firm's system of quality management, and parties that are external to the firm. As part of strengthening the linkage to ISQC 1, the Task Force is of the view that highlighting the overarching requirement for effective two-way communication in the introductory paragraphs is important (see new paragraph 2B in **Agenda Item 5-B**). Further changes related to communication, including addressing the necessary information required to be communicated and to whom, as well as highlighting the responsibilities of the EP and ET to communicate effectively and on a timely basis have also been considered by the Task Force and are discussed further in Section D below.

Matters for IAASB Consideration:

1. The IAASB is asked to share its views on the revised introductory paragraphs 2–3A in the introductory paragraphs of ISA 220 (see **Agenda Item 5-B**), in particular:
- (a) That it should be made clear that the EP may assign procedures to others to assist the EP in fulfilling his or her responsibilities.
 - (b) Whether the link to ISQC 1 has been clearly made.

17. ISA 220 also interacts with activities addressed by other ISAs that are also applicable at the planning stage of an audit. It is the view of the Task Force that these interactions need to be highlighted more prominently in the introductory paragraphs as information learned from addressing requirements in other ISAs will be relevant to addressing the requirements of ISA 220. The Task Force also notes that as the audit progresses, additional information may become available that may also affect managing quality at the engagement level. The Task Force therefore proposes adding references to the following ISAs in the introductory paragraphs:

- ISA 210⁹—deals with the auditor's responsibilities in agreeing the terms of the audit engagement, including the preconditions for an audit as well as understanding if there will be limitations on the scope of the engagement.
- ISA 300¹⁰—Paragraph 2 of ISA 300 describes how an audit involves establishing the overall audit strategy for the engagement and developing an audit plan, and highlights ways in which adequate planning benefits the audit engagement. The matters listed in this paragraph include those that are addressed by ISA 220. Additionally, paragraphs 6 and 13 of ISA 300 addresses preliminary engagement activities and makes reference to the required procedures relating to acceptance or continuance of client relationships and the specific audit engagement, and compliance with relevant ethical requirements, all in accordance with ISA 220. Some matters set out in paragraph 8 of ISA 300 also make reference to matters that would also be considered in ISA 220 (e.g., resources necessary for the engagement). Paragraph 10 of ISA 300 deals

⁹ ISA 210, *Agreeing the Terms of Audit Engagements*

¹⁰ ISA 300, *Planning an Audit of Financial Statements*

with the need to plan the nature, timing and extent of direction and supervision of ET members and the review of their work and the related application guidance also refers back to ISA 220.

- ISA 315 (Revised)—although no specific reference is currently made to ISA 220 in ISA 315 (Revised), information relevant to managing quality at the engagement level is also relevant to the process of identifying and assessing risks of material misstatement through understanding the entity and its environment and its internal control (for example, information gathered and considered during client and engagement acceptance or continuance). Similarly, performing further audit procedures in response to the risks of material misstatement will also affect or be relevant to how quality is managed overall (for example, through a need to include individuals with particular skills or expertise in the ET, or to take a particular approach to direction and supervision for a particular area).
18. The interaction of ISA 220 with ISA 210, ISA 300 and ISA 315 (Revised) suggests that acceptance or continuance and other aspects of managing quality are not isolated from planning the audit engagement in terms of ISA 300 and ISA 315 (Revised), and that this process is not linear. The Task Force is also of the view that it is important to recognize that information obtained in fulfilling the requirements of each of the various applicable standards is not isolated, and that the understanding of the entity and its environment is applicable to more than one standard. The Task Force believes that these inter-relationships among the standards should be made clearer in ISA 220 and the other standards. In addition to the proposed amendments to the introductory paragraphs of ISA 220, conforming amendments may also be necessary to ISA 300 and ISA 315 (Revised), for example to make it clear that the requirements of the applicable ISAs may be addressed simultaneously, and involve an iterative process, and that aspects of obtaining an understanding of the entity and its environment are relevant to addressing multiple requirements within the ISAs. It is intended that application material be developed to provide examples of information that may be applicable to the various aspects of accepting or continuing the engagement and planning the audit (see revised paragraph 3B of ISA 220 in **Agenda Item 5-B**).

Matter for IAASB Consideration:

2. The IAASB is asked whether making the links to other relevant ISAs in the introductory paragraphs 3B–3D (see **Agenda Item 5-B**) is helpful for explaining the interactions between the standards, and whether additional references need to be considered to highlight interactions with any other standards.

B. Quality Management at the Engagement Level

19. The overarching objective of ISA 220 is related to the effective management of quality at the engagement level, and a key aspect is the establishment of the responsibility of the EP for the audit engagement and its performance. The responses to the ITC highlighted the need for more emphasis on, and clarity about, the responsibilities of the EP.
20. The objective of the auditor has not been substantially amended, other than revising the terminology to refer to quality management. The objective also remains consistent with the objective of ISQC 1 (See paragraph 6 of **Agenda Item 5-B**). In revising this paragraph the Task Force also proposes that the overall objective could also more explicitly encompass “achieving” quality, i.e., noting that “managing quality” may be read by some as not necessarily encompassing a quality outcome.

However, the Task Force will continue to deliberate what the most appropriate language to achieve this objective is, as well as remain coordinated with the QCTF in this regard.

21. To be consistent with the revision of ISQC 1 to integrate a QMA, and as discussed above, the Task Force is of the view that ISA 220 should also incorporate quality management principles at the engagement level. The Task Force has extensively explored what 'quality management at the engagement level' means and how quality management principles can be introduced into ISA 220.
22. The revisions being explored in relation to ISQC 1 and extant ISA 315 (Revised) approach quality management and the audit respectively through a process that, among other things, involves identifying and assessing risks (i.e., quality risks or risks of material misstatement) and responding accordingly. The Task Force has previously considered whether and how to introduce a risk assessment process for quality management at the engagement level—an approach to managing quality at the engagement level through quality risk identification and assessment for the individual engagement was preliminarily explored with the IAASB at its December 2016 meeting (see paragraphs 46–53 of [Agenda Item 8–A](#) of the December 2016 IAASB meeting materials). The IAASB expressed caution about the proposed approach, noting the potential confusion that might be created through the introduction of yet another discrete risk assessment process at the engagement level, and questioned how such a process would align or intersect with the existing risk assessment process that is the foundation of ISA 315 (Revised) and ISA 330¹¹ (i.e., focused on identifying, assessing and responding to risks of material misstatement at the financial statement and assertion level). The IAASB encouraged the Task Force to further consider how quality management could be embedded at the engagement level.
23. Extant ISA 220 sets out the requirements for the aspects of quality control that are required to be addressed in an audit (i.e., the core elements of ISA 220). Each of these core elements is initially addressed by the firm in extant ISQC 1 (i.e., the 'elements of a system of quality control'), with ISA 220 setting out how these are applied specifically in audit engagements. These core elements include:
 - Relevant Ethical Requirements.
 - Acceptance and Continuance of Client Relationships and Audit Engagements.
 - Assignment of Engagement Teams.
 - Engagement Performance (including direction, supervision and performance; reviews; consultation; engagement quality control review and differences of opinion).
 - Monitoring.
24. Instead of proposing the introduction of an overarching requirement to perform a quality risk assessment at the engagement level, the Task Force is of the view that building quality management into an individual audit engagement would most effectively be accomplished by embedding quality management principles into each core element of ISA 220.
25. The QCTF are exploring how the new requirements to establish quality objectives, and identify quality risks and responses can be practically applied to the quality elements in extant ISQC 1 (which are aligned with the ISA 220 core elements set out in paragraph 23 above). In developing the prescribed

¹¹ ISA 330, *The Auditor's Responses to Assessed Risks*

quality risks and responses, the QCTF have retained the existing requirements within the elements in ISQC 1, albeit that they have been restructured as either quality risks or responses. **Agenda Item 2-C** sets out the QCTF's initial proposals regarding the prescribed quality objectives, quality risks and responses and includes alternative forms of presentation for the IAASB to consider. As explained in paragraphs 81-82 of **Agenda Item 2-A**, the QCTF is considering whether the quality objectives, quality risks and responses should be categorized according to the elements that exist in extant ISQC 1.

26. The Task Force believe that the core elements of extant ISA 220 (as set out in paragraph 23 above) should be retained, as they are integral to an effective approach to managing quality at the engagement level. The Task Force also views the retention of the core elements as important in retaining the rigor of the extant standard. Even though the core elements may not be articulated as discretely in the revised ISQC 1, the Task Force also notes that these elements would however be established initially by a firm as part of addressing the ISQC 1 requirements (i.e., as part of implementing and operating the firm's system of quality management).
27. The Task Force has also considered, in light of the changes being made to ISQC 1, whether there are other core elements that need to be addressed at the engagement level, but is of the view that the overall core elements are complete (and consistent with what is described in extant ISQC 1 and ISA 220) and there is no need for further change. However, the Task Force believes that there are aspects of the core elements that need to be further considered and clarified. These views are reflected in the changes that have been proposed and explained further in Section D below. The Task Force will continue to monitor developments in ISQC 1, and as the changes to ISQC 1 are finalized, the Task Force will continue to consider whether the proposed approach of continuing to use the core elements in ISA 220 as the structure for the standard requires reconsideration.
28. The Task Force is of the view that the most effective way to embed quality management principles at the engagement-level is through establishing a 'four-step approach' that sets out the steps that would need to be addressed for each core element, including appropriate responses based on engagement facts and circumstances. This approach would also include an overarching requirement (or stand-back) for the EP to consider whether there is anything else that would cause quality to not be achieved for that audit engagement, and if so, to take action to implement an appropriate response.
29. As noted above, quality management at the engagement level is performed in the context of the firm's quality management system (i.e., addressing the requirements of ISQC1). The firm will have set quality objectives and identified quality risks in relation to those objectives (including risks related to audits of financial statements), and will have designed responses to those risks.
30. Accordingly, at the engagement level, for each core element and in light of the specific engagement's facts and circumstances, the EP should understand the applicable firm-level policies or procedures and consider what the firm has put in place (including what is expected at the engagement level) to address quality risks for the engagement. As well as adding more specificity about the EP's responsibilities to the various elements in ISA 220, the Task Force is of the view that applying a four-step approach that address the EP's responsibilities will help reinforce and clarify the overall responsibility of the EP for the audit.
31. Therefore, the Task Force proposes that the section of ISA 220 that sets out the EP's overall responsibilities for the engagement would be expanded to include the four-step approach, and that the approach be applied in addressing each of the core elements of ISA 220. The four-step approach

would effectively require the EP to understand, for each core element, what could go wrong such that quality would not be achieved, and to put in place actions to address those risks to quality. The four-step approach to be applied to each core element of ISA 220 would address the EP's responsibilities to:

- **Understand** what the firm's policies or procedures are that are relevant to the engagement for the core elements. This approach would:
 - Build on the firm's system of quality management required by ISQC 1 for the firm based on the firm's identification and assessment of risks to quality and the firm's responses; and
 - Focus the EP on those aspects of quality management that are relevant to the engagement, and on the EP's responsibilities for taking action in this regard at the engagement level.
- **Determine** whether the firm's policies or procedures are **sufficient and effective**¹² for that particular engagement, including understanding whether the firm's policies or procedures are effectively designed, operating as intended, and whether they are sufficient for the particular engagement, or whether incremental actions are necessary). EP's would also need to consider any impact or outcome of the responses undertaken at the firm level for the engagement (for example, the outcome of the firm's independence monitoring procedures on the engagement acceptance or continuance decision).
- **Respond** to risks to quality for the audit by taking action to address the risks to quality as appropriate and in the context of the particular element. The EP would implement the firm's policies or procedures at the engagement level, and other incremental responses as deemed necessary by the EP. Developing appropriate responses at the engagement level will involve professional judgment and the exercise of professional skepticism, and would be based on the facts and circumstances of the engagement—for example, the more complex and difficult the engagement, the more involved or detailed the response may need to be at the engagement level and the more the personal involvement of the EP may be required. The Task Force is also of the view that developing appropriate examples to be included in the application guidance would also provide an opportunity to demonstrate how professional skepticism may be applied.
- **Communicate** as appropriate with the firm (e.g., ask for more information from the firm or provide feedback to the firm where necessary), with members of the ET and others involved in the audit and with external parties as appropriate.

32. For example, the firm may identify risks to audit quality related to the challenging implications of a new accounting standard for an industry. The firm therefore establishes a requirement for audit engagements in that industry to be subject to independent reviews by an industry expert of risk assessment and planning, prior to the commencement of the planned further audit procedures. The firm includes this new requirement in its audit manual and communicates with its personnel through an announcement in its weekly technical bulletin and by highlighting the new accounting standard

¹² Assessing effectiveness would not suggest that the 'operating effectiveness' (as described in the risk assessment standards) needs to be tested by each ET. Application material would be added to explain however that the EP or ET cannot just assume that the firm's response is sufficient and effective, and would provide examples of how an EP or ET can determine that firm-level policies or procedures are effective.

requirement in the technical training session that is mandatory for all audit personnel. In this case, the EP for an audit in that industry would have responsibility for understanding that the engagement is subject to the new requirement, for determining that an appropriate independent reviewer has been assigned to the engagement, for co-operating with the reviewer and for making sure that the review is complete and the related comments addressed before the ET commences with the planned audit procedures.

33. The application of the four-step approach to each of the specific core elements of 220 is discussed further in Section D below.
34. Once all core elements have been considered and addressed, the Task Force is of the view that the EP should perform a ‘stand-back’ evaluation on whether all of the quality risks have been addressed or whether there are any incremental risks, and take further action as appropriate. This evaluation is further discussed in paragraphs 80 to 83 below.
35. The Task Force is of the view that the four-step approach and overall stand-back, although not prescribed by the requirements addressing the elements in extant ISA 220 currently, is likely to be implicitly or explicitly applied in practice today by many firms. Such a new approach will also necessitate enhanced documentation requirements; however these will be considered by the Task Force once the Board's views on the proposed approach have been obtained. Such In addition to being helpful to the auditor in determining how the risks to quality have been identified and addressed at the engagement level, enhanced documentation requirements will also provide the appropriate basis for audit oversight bodies and other reviewers to understand how the requirements of ISA 220 have been addressed, and the objective of the standard achieved.
36. Changes to reflect the Task Force views are further described in this paper below, including initial thinking as to how the four-step approach would be reflected in the requirements to address each of the core elements and the introduction of a communication and information section. Board members should note that the proposed revisions to incorporate the four-step approach into the requirements addressing the core elements of ISA 220 represent initial thinking by the Task Force and are intended to illustrate for the board how the approach might be incorporated. The Task Force is aware that additional refinement and clarification will be necessary. In progressing its work, the Task Force will be mindful of the changes being developed in ISQC 1, and will also bear in mind the responses to the ITC. The Task Force is of the view that the proposed approach and related revisions would demonstrate the importance of proactive quality management at the engagement level, retain the current rigor in ISA 220, and also incorporate the robust changes being made in ISQC 1 to requirements for managing quality at the firm-level.

Matters for IAASB Consideration:

3. The IAASB is asked for its views on the ‘objective’ of the auditor as described in paragraph 20. i.e., whether the objective is to ‘manage’ engagement quality or ‘manage and achieve’ engagement quality.
4. Does the overall approach described in Section B above appropriately embed quality management principles in ISA 220, thereby effectively responding to calls for enhancing audit quality at the engagement level?

C. The Overall Responsibility of the Engagement Partner for the Audit

37. As explained above, in order to entrench quality management principles and more clearly link the EP's considerations at the engagement level to what the firm has in place, a four-step approach to guide the EP's considerations in relation to understanding what could go wrong in relation to quality for each core element would be established (see paragraphs 30–31 above). The Task Force is also of the view that an emphasis on the need for timely information and communication as part of the EP's responsibilities would also help entrench the revised requirements in ISA 220 (see further discussion relating to communication in paragraphs 42–51 below). Revised paragraph 8 in **Agenda Item 5-B** sets out the proposed overall framework that will assist the EP in achieving the objective for managing quality of the engagement. The revised requirement also makes clear that managing quality is achieved through addressing the other requirements in the standard, i.e., as they relate to the core elements.
38. In order for EPs to be able to assess risks to quality for the engagement and determine whether the responses to those risks are sufficient and effective, EPs will need to have an understanding of the entity and its environment and the circumstances of the engagement that is sufficient to be able to discharge these responsibilities. Therefore the Task Force is of the view that a new requirement should be added that sets out the requirement for the EP to have an understanding of the nature of the entity and its circumstances as the foundation for addressing the requirements of this ISA. See new paragraph 8A in **Agenda Item 5-B**. This new requirement involves designing an appropriate approach to the direction, supervision and review of the engagement, i.e., to form the basis for the conclusion that the EP's involvement has been sufficient to support the conclusion that quality has been effectively managed and achieved.
39. The Task Force proposes that application material be developed to provide guidance on the types of matters that would form the basis of the understanding referred to in new paragraph 8A, such as an understanding of the nature of the entity (e.g., whether it is a business enterprise, a public sector entity or a not-for-profit organization) and the industry in which it operates (some industries require specific expertise); the relevant applicable financial reporting framework and how it is applied to the entity (including any specific complexities that arise); the organization and structure of the entity; and applicable laws and regulations. In practice, some of this information may already have been obtained (or may be in the process of being obtained or updated) in order to meet various requirements of ISQC 1, ISA 210, ISA 300 or ISA 315 (Revised). The new requirement proposed for ISA 220 is intended to make sure that the EP has the relevant knowledge about the engagement to form the basis for designing the approach to managing and achieving quality at the engagement level and acknowledges that some of the information for the required understanding may have been obtained by others (e.g., others might have obtained relevant information in accepting or continuing the client or engagement and it is important that knowledge of such information be appropriately communicated to the EP and other team members as necessary).
40. Further, the Task Force is of the view that greater clarity around the responsibilities of the EP could be provided through new application material being included throughout the standard, such as:
- Examples of how specific policies or procedures at the firm level may mitigate risks to quality for the engagement such that no further action may be needed at the engagement level. For example, identified risks to quality may be mitigated by firms requiring an engagement quality control (EQC) reviewer or other reviewers for certain high-risk clients, and therefore the EP

may conclude that no further reviews by individuals outside the ET are needed at the engagement level.

- Examples of engagement-specific actions to address engagement-specific risks, such as seeking consultation for an area where the firm does not specifically require consultation. For example, the entity may own assets in a jurisdiction that the ET is unfamiliar with, and an impairment test is required—the ET may want to consult with appropriate resources within the firm or in a network firm in the jurisdiction to determine that appropriate indices have been used in the related assumptions, and that the impairment assessment is appropriate in the context of the jurisdiction’s environment.

Matters for IAASB Consideration:

5. The IAASB is asked for its views on:
- (a) The four-step approach to be applied in addressing each of the core elements of ISA 220 set out in paragraph 31.
 - (b) Whether the core elements of ISA 220, set out in paragraph 23, are still relevant and should be retained, and whether these are complete (i.e., are there other elements or quality risks that should be addressed by the requirements of ISA 220).
 - (c) Whether the four-step approach for embedding quality management principles as presented in revised paragraph 8 of ISA 220 (see **Agenda Item 5-B**) effectively clarifies the overall responsibility for the EP? Is it clear that the overall requirement would be achieved through meeting the requirements in ISA 220, including those that address the core elements and the proposed ‘stand-back’?
 - (d) The new requirement for the EP to obtain a preliminary understanding of the engagement in order to be able to address the requirements of ISA 220 (see new paragraph 8A in **Agenda Item 5-B**).

D. The Core Elements to be Addressed on All Audits

41. In addition to revising the approach to each core element to incorporate the four-step approach set forth in Section B above, the Task Force has also discussed whether aspects of each core element require restructuring and strengthening (for example, where the respondents to the ITC indicated that a particular aspect should be strengthened or further considered). This section of the Issues Paper sets out the Task Force views on possible changes to ISA 220. Initial thinking on revised drafting for the relevant requirements can be found in **Agenda Item 5-B**.¹³

Information and Communication

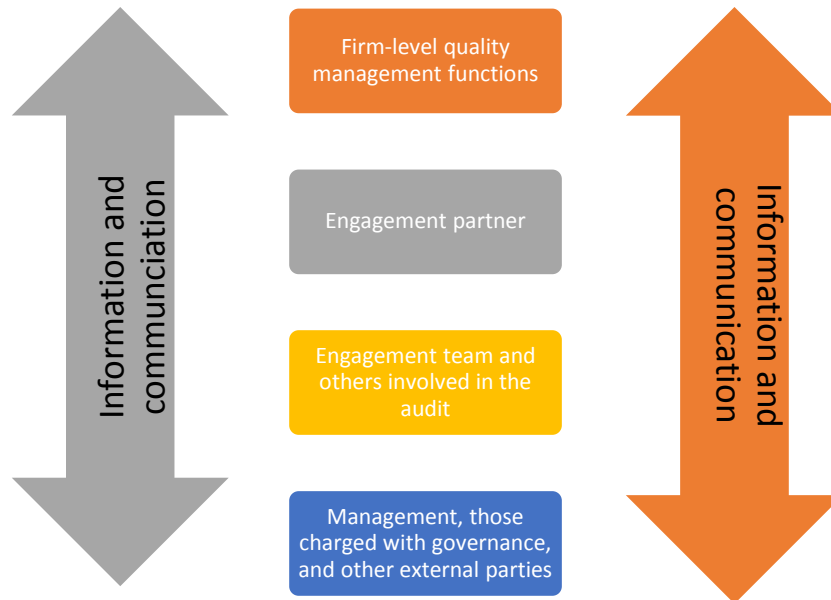
42. Although not directly highlighted as part of the responses to the ITC relating to ISA 220 (the issues relating to communication had mainly been presented relating to group audits), communication between the group ET and component auditors was highlighted by many respondents to the ITC as

¹³ The revised drafting for each of the below core elements in ISA 220 represents the Task Force’s progressed thinking and is subject to further clarification and refinement. However, what is presented in **Agenda Item 5-B** is intended to assist the Board in further understanding the Task Force’s proposed approach, including how the four-step approach described in section B above might be applied to each of the core elements.

an area where requirements needed to be strengthened. It was noted in the responses related to group audits that two-way communication at all stages of the audit would among other things, enable the group ET to (1) better understand if the instructions provided to the component auditor had been fully understood and that the component auditor was capable of complying with them, and (2) have an improved basis for concluding that sufficient appropriate audit evidence relating to the engagement has been obtained. The Task Force is of the view that this feedback and the related principles are also relevant and should be applied to communications between and among the EP and the ET and any others that might be involved in the audit, as well as between the EP and the firm.

43. In addition, the QCTF has developed new enhanced proposed requirements in ISQC 1 related to information and communication for the firm. The proposed draft of ISQC 1 identifies the various information sources and stakeholders with whom two-way communication may take place, including the ET, personnel performing functions in relation to the operation of the firm's system of quality management, firm leadership and parties external to the firm.
44. In light of the increased focus in ISQC 1 on enhanced communication and information, the Task Force's possible enhancements that were discussed by the IAASB in December 2016 included a new proposed requirement for ISA 220 for ongoing, two-way communication among the members of the ET, others involved in the engagement, and the firm and related application guidance (e.g., the EP may communicate resource requirements back to the firm as and when needed or where risks to quality are identified that need to be communicated back to the firm for action at the firm level). The Task Force believes that effective communication among the ET and others involved in the audit sets the foundation for an effective and efficient audit, and helps the EP determine the level of necessary involvement in the audit and the nature, timing and extent of appropriate direction, supervision and review.
45. Board members supported a new requirement in ISA 220 to address communication. However, members cautioned that the proposed new requirement may be overly prescriptive or limiting and may promote a "check-box" mentality. Taking into account the feedback provided by Board members, the Task Force continues to believe that requirement for communication is important, and particularly where the members of the ET are more distributed and involve individuals working in different locations who communicate more on a virtual basis (e.g., where audit delivery models (ADMs) are involved and in situations where the EP is not situated where the majority of the audit work is performed). Further, the Task Force believes that effective communication is the foundation for achieving appropriate direction, supervision and review. Accordingly the Task Force has revised the new proposed requirement to require and promote effective communication among the firm, the EP and the ET (see new paragraph 8B in **Agenda Item 5-B**).

46. The illustration that follows demonstrates how the Task Force believes the movement of information from the firm down to the ET (and back up) should operate in order to ensure effective communication and ultimately lead to effective management of quality for an audit of financial statements.



47. The Task Force proposes including language in the requirement to clarify that it is the EP's responsibility to communicate information pertaining to quality management at the engagement level that may be relevant to the firm's system of quality management to the appropriate individual(s) within the firm. Likewise, relevant information received about the firm's system of quality management that is relevant to quality management at the engagement level is required to be communicated by the EP to members of the ET or others involved in the audit. These proposed changes also address making such communications on a timely basis. The proposed changes are intended to strengthen the two-way communication relating to matters relating to the firm, such as about the importance, relevance and benefits of the firm's quality management, and about internal and external inspections as relevant (see additional potential application material below).
48. The Task Force also proposes the addition of a requirement that the EP direct the other members of the ET, and others involved in the audit, to communicate information that may be relevant to management of quality at the engagement level to the EP on a timely basis. Consideration will be given to including examples in the application material of the types of communications that this requirement might address.
49. The approach set out above to strengthen the requirements around communication is integral to the Task Force's approach to quality management at the engagement level as described in section C above, and is designed to change behavior at the engagement level.
50. The Task Force will continue to monitor the changes in ISQC 1 (and ISA 600 as relevant) relating to communication to ensure that there is alignment and consistency between the new and revised requirements. For example, the Task Force has currently reflected in its proposed enhancements revisions to the title of this requirement to include "information" to reflect the changes being proposed

in ISQC 1. Conforming wording adjustments will likely be an iterative process as the two projects are progressed.

Application Material

51. As the requirements are further developed, the Task Force is of the view that these could be further supplemented by application material providing examples of appropriate communications in various situations and by describing the different relationships that may exist (specifically within the ET and/or with external parties). The Task Force has progressed its thinking in this regard. For example, the Task Force sees merit in including additional application material that:

- Encourages the communication of appropriate information related to the firm’s system of quality management (and communicated by the firm) by the EP to the appropriate members of the ET.
- Encourages communication by the EP about matters relating to the engagement that may be relevant to the firm’s system of quality management to the appropriate individuals within the firm responsible for the firm’s system of quality management.
- Provides examples of matters that may be communicated from the firm to the ET,¹⁴ such as:
 - Information related to the firm’s culture, for example, the message that each individual has a personal responsibility for quality and is expected to comply with the firm’s policies or procedures.
 - The firm’s responses to quality risks, for example, policies or procedures in relation to the firm’s system of quality management that ETs are expected to apply at an engagement level (e.g., the firm’s policies or procedures in relation to acceptance and continuance of engagements).
 - Information that describes the authority, roles and responsibilities of personnel performing functions in relation to the engagement.
 - Information related to monitoring and remediation, for example, relevant information about the results of the firm’s monitoring and remediation.

Application guidance could also address the matters that would need to be communicated back to the firm from the ET.

- Includes examples to address timely communication and illustrate interactive communication, as the auditor plans, performs and assesses the work performed, between the EP and ET (and any others involved in the engagement), but in particular for situations where other auditors are used, including ADMs and situations where the EP is not situated where the majority of the audit work is performed.
- Sets out the appropriate types of communications that may be appropriate in different situations, for example in-person, telephonic, in a virtual form, written confirmations, etc.

¹⁴ The bullets below are consistent with ISQC 1 as redrafted, see paragraph A38 of **Agenda Item 2-B**.

- Links back to the documentation requirements in ISA 230¹⁵ regarding communications.

Relevant Ethical Requirements (Including Independence)

52. Although the Task Force did not present proposed enhancements to requirements addressing this core element at the Board's December 2016 meeting, it has continued to consider the impact of introducing the approach to managing quality into the EP's considerations about ethical requirements.
53. The Task Force also discussed the need for revisions to ISA 220 in light of changes arising from revised requirements about the auditor's considerations about non-compliance with laws or regulations (NOCLAR) in both the IESBA Code of Ethics for Professional Accountants (IESBA Code) and ISA 250 (Revised).¹⁶ The Task Force also considered that the QCTF is discussing expanding the relevant ethical requirements in ISQC 1 to other areas (e.g., professional behavior) and that those changes, once discussed with the Board, will need to be reflected in ISA 220 accordingly.
54. The Task Force has currently proposed no changes to the extant requirement in paragraphs 9 and 11, but agrees that additional application material to the requirement would be helpful (see below).
55. However, the Task Force notes that it is not sufficiently clear within paragraph 10 of ISA 220 that the EP may obtain information from other sources (possibly outside of the firm) related to compliance with ethical requirements. Accordingly, the Task Force is of the view that this requirement could be clarified in this regard. (See proposed changes to paragraph 10 in **Agenda Item 5-B**).

Application Material

56. The Task Force is of the view that the relevant ethical requirements could be further supplemented by additional application material to paragraph 9 to emphasize the broader aspects of relevant ethical requirements (i.e., broader than the specific focus in extant ISA 220 and ISQC 1 on independence). This new application material could include examples:
 - Of what could be considered as non-compliance with the ethical requirements, e.g., a failure to identify and address an instance of NOCLAR either by the entity or by the ET.
 - Relating to professional behavior and long association.

In addition, examples of the EP and ET's considerations when firm-level policies related to ethical requirements are expected to be executed at the engagement level (e.g., on-the-job training and other communications to raise awareness of the importance of compliance with ethical requirements) could also be added.

¹⁵ ISA 230, *Audit Documentation*, paragraph 8(a) requires "documentation of compliance with the ISAs" and the accompanying application material to this requirement, A7, goes further to explain that "Audit documentation provides evidence that the audit complies with the ISAs. However, it is neither necessary nor practicable for the auditor to document every matter considered, or professional judgment made, in an audit. Further, it is unnecessary for the auditor to document separately (as in a checklist, for example) compliance with matters for which compliance is demonstrated by documents included within the audit file. For example:...In relation to requirements that apply generally throughout the audit, there may be a number of ways in which compliance with them may be demonstrated within the audit file:... that the engagement partner has taken responsibility for the direction, supervision and performance of the audit in compliance with the ISAs may be evidenced in a number of ways within the audit documentation. This may include documentation of the engagement partner's timely involvement in aspects of the audit, such as participation in the team discussions required by ISA 315 (Revised)."

¹⁶ ISA 250 (Revised), *Consideration of Laws and Regulations in an Audit of Financial Statements*

57. The Task Force discussed adding the following additional application guidance to clarify what is meant by certain phrases within the extant requirement in paragraph 10 including:
- Explaining what is meant by ‘other sources’ and give examples of what those sources could be. For example, other sources may be in relation to other information that the auditor comes across, other individuals that provide information, etc.
 - Describing what is meant by ‘appropriate action,’ and that it could be one or more of the following:
 - A specific response at the engagement level, which would involve communication within the ET;
 - A specific response at the firm level, which would involve the need for communication with those individuals within the firm responsible for the system of quality management; or
 - A specific response at the network level, which would involve the need to communicate to the network and could involve the need to communicate with external parties.
58. The Task Force is also aware that changes are currently being made to the IESBA Code, and will continue to monitor these changes for any impact on ISA 220. The Task Force also remains mindful that proposed changes to ISA 220 could have implications on the IESBA Code, and therefore continues to consider the possible impact of the proposed changes in ISA 220 on the IESBA Code, if any. The Task Force will coordinate with the IESBA, as relevant, on matters of mutual interest as the revisions to ISA 220 are further developed.

Matters for IAASB Consideration:

6. The IAASB is asked for its views on the new requirement for enhanced information and communication as set out paragraph 8B in **Agenda Item 5-B**, including in light of the changes being proposed in ISQC 1.
7. The IAASB is asked for its views on the matters and possible actions, relating to relevant ethical matters, set out in paragraph 52–58 above.

Acceptance and Continuance of Client Relationships and Audit Engagements

59. The Task Force has proposed changes to the requirements addressing acceptance and continuance of an audit engagement that attempt to introduce the four-step approach for managing quality at the engagement level. Further changes will be necessary to directly align the requirements with the proposed revisions to ISQC 1 in relation to this element once ISQC 1 has been finalized.
60. Neither ISQC 1 nor ISA 220 specify which individuals should be assigned responsibility for making the decision to accept or continue an engagement—the firm’s policies or procedures relating to this element would likely specify who should be involved, and may also have graduating levels of required approvals depending on the nature and size of the engagement. In practice these policies or procedures would vary and the designated individual(s) could be a senior leader within the firm or designee, the EP assigned to the engagement, or a combination. If the EP makes the initial conclusion, this may be subject to approval by others within the firm. The Task Force is of the view that the standards need not prescribe who makes the decision to accept or continue the engagement.

Nonetheless, in accepting responsibility for the engagement to which the EP has been assigned, the EP, in considering risks to quality at the engagement level related to this element, should take responsibility for understanding the firm’s policies or procedures and how they have been applied in the context of a particular engagement, and determine whether there is anything more that needs to be addressed, or whether there is information that should be communicated to the firm or others. See proposed revisions to paragraph 12 and suggestions for related application guidance set forth in **Agenda Item 5-B**.

61. The Task Force also discussed the requirement in paragraph 13 to communicate information promptly should circumstances arise during the audit that would have caused the firm to decline the audit engagement if that information had been known earlier, and agreed that it was important to maintain this requirement. The Task Force proposes amending this requirement to make it clear that this communication should take place in a timely manner. See proposed revisions to paragraph 13 in **Agenda Item 5-B**.

Matter for IAASB Consideration:

8. The IAASB is asked for its views on the proposed revisions to paragraphs 12 and 13 in **Agenda Item 5-B**. In particular, is it clear what procedures need to be undertaken to comply with this revised requirement? Is there any additional application material that should be considered by the Task Force?

Determination of Engagement Resources, Including Assignment of Engagement Teams

62. Extant ISA 220 sets out the requirements related to the ‘assignment of the engagement team.’ In revising ISQC 1, the QCTF has considered a broader range of resources that may be required for enhancing the quality of engagements. The QCTF is considering broadening the requirements and application material in relation to the firm’s maintenance of sufficient and appropriate resources that are necessary for the proper functioning of the firm’s system of quality management and for the performance of engagements. These include financial resources, human resources, technological resources and intellectual resources. The Task Force has agreed that that the corresponding requirements in ISA 220 should also be broadened to require consideration of more than only the assignment of the ET, i.e., to include consideration of a broader range of resources as appropriate at the engagement level, and maintain consistency with the strengthening of ISQC 1. At its December 2016 meeting, the Board supported the following proposed enhancements to this requirement:

- Revise the title of this section to clarify the EP’s responsibility for consideration of all resources related to the audit, e.g., ET members (including any other auditors at network firms or ADMs), auditor’s experts, automated audit technologies, other data analytics software required, etc.;
- Broaden the requirement by replacing the phrase “engagement team, and any auditor’s experts who are not part of the engagement team, collectively have the appropriate competence and capabilities” with “audit engagement has the appropriate and adequate resources necessary to:...” i.e., broadening the EP’s responsibilities for ensuring that the assignment of the ET includes all aspects of resources needed for the audit.

63. The Task Force proposes adding a new requirement to ISA 220 (existing paragraph 14 will become part of new paragraph 14A) to introduce the four-step approach for managing quality discussed in Section B above, and to enhance the requirement to include consideration of all resources needed

for the engagement (see new paragraph 14 in **Agenda Item 5-B**). This proposed change will address feedback provided by the Board to broaden the requirement to include all resources (including technology) for the engagement. Application guidance with different examples of the types of resources that could be considered could be developed to support the new and expanded requirement.

64. The Task Force proposes retaining the focus on the competence and capabilities of the members of the ET and any experts who are not part of the ET addressed by extant paragraph 14 in ISA 220. Additionally, controls over the use of technology tools is a relevant and important issue highlighted by the Data Analytics Working Group, as well as by numerous stakeholders. Focusing on these matters was initially discussed with the IAASB at its December 2016 meeting, and based on feedback from the Board, the Task Force added paragraph 14A (see **Agenda Item 5-B**) to reflect the continuing focus on the competence and capabilities of those involved in the audit, and methodologies or technologies (i.e., that they are available and appropriate, including that the ET members have the appropriate skills and experience to use them as intended). The Task Force understands that some tools within the firm are required to be used by all audit ETs, or by certain ETs where the audits have certain attributes, and has proposed the changes within the requirement to reflect this. In these cases, if the firm mandates the use of a particular tool, the firm would be expected to also develop policies or procedures around its use (e.g., in training programs) in order to ensure that audit quality can be achieved on each engagement. The EP has a responsibility to understand firm expectations in respect of the tool, including the objective of the tool, when it should be used, how it works, and if it works, what the expectations are for what needs to be done at the engagement level to support the proper application of the tool (for example, certain engagement specific parameters or inputs may need to be determined by the ET.) Application material would also be developed to provide additional examples of the application of this requirement.

Matter for IAASB Consideration:

9. The IAASB is asked for its views on revised paragraph 14 in **Agenda Item 5-B**. In particular, is it clear what procedures need to be undertaken to comply with this revised requirement? Is there any additional application material that should be considered by the Task Force?

Engagement Performance

Direction, Supervision, Performance and Reviews

65. As discussed in paragraph 15, the Task Force believes that a foundational component of managing quality for an audit engagement is that the EP is sufficiently involved in the engagement in order to have a basis for demonstrating how the objective of ISA 220 has been met. The level of the EP's involvement in the engagement will be a function of the nature, timing and extent of direction, supervision and review, which will therefore be the basis for determining that the EP was indeed "sufficiently involved." This determination will be a matter of professional judgment and will depend on the facts and circumstances of the engagement. The EP's understanding of the entity and its environment, as well as consideration of the other core elements of ISA 220 and how they are being addressed will also help inform the appropriate level of involvement necessary in order to support the conclusion that the EP's involvement was sufficient.

66. In extant ISA 220, the requirements set out that the EP shall take responsibility for the direction, supervision and performance of the engagement,¹⁷ and for the necessary reviews to be undertaken in accordance with firm policies or procedures.¹⁸ At the Board's December 2016 meeting, it was proposed that the requirements that are currently in paragraphs 15 and 16 of ISA 220 be rearticulated and combined into one requirement, supported by the development of additional supporting application material addressing relevant considerations relating to the nature, timing and extent of the EP's involvement in the audit, and by revising the section title to be "Direction, Supervision, Performance, and Reviews." Comments and feedback from the IAASB's discussion at its December 2016 meeting included:
- Overall support for the direction of the proposed revisions to the requirements and application material.
 - A suggestion to include considerations that would encourage appropriate application of professional skepticism in the examples in the application material.
 - A call for considering more specificity about how direction and supervision should be undertaken, including in situations where the ET is not all in one location.
67. The Task Force is of the view that the performance of the engagement is a collective responsibility of the ET, with the EP taking overall responsibility for the work performed. Performing the work effectively and efficiently therefore involves appropriate direction, supervision and review by the EP but also likely by other members of the ET, or others involved in the audit. The plan for appropriate direction, supervision and review therefore is a function of, and needs to be responsive to, the risks to quality that have been identified when accepting or continuing and planning the engagement. The Task Force is also of the view that the application material to extant paragraph 14 in ISA 220 should highlight that the EP may make assignments to other members of the ET and others involved in the audit, but emphasizing that the EP retains overall responsibility and should have appropriate involvement throughout the engagement in order to be sufficiently involved, i.e., from planning to completion. This will also help explain and link back to new paragraph 3A (see **Agenda Item 5-B**) in the introductory section to the standard.
68. In revising the requirement for the direction, supervision and review of the engagement, the four-step approach for managing quality has been used to embed the quality management principles in this process (see new Paragraph 15A in **Agenda Item 5-B**). The Task Force has also debated how to demonstrate the different responses to risks to quality in the standard, while keeping the requirements principles based, and believes that describing factors that impact the nature, timing and extent of the direction, supervision and review of the engagement will be helpful. Examples of the factors that could be considered include:
- The nature of the entity (including its size and complexity), and the nature of the environment within which it operates;
 - The nature of the ET and how it is organized (e.g., whether the ET is located at a single location or at multiple locations, whether an ADM is involved, whether other auditors or component auditors are involved);

¹⁷ ISA 220, paragraph 15

¹⁸ ISA 220, paragraph 16

- The capabilities and competence of the members of the ET and others involved in the audit (i.e., the knowledge, skills and ability of each ET member) including those that have responsibility for direction, supervision and review of other team members;
 - The nature, timing and extent of the audit procedures to be performed, e.g., more complex areas may require more hands-on, and more extensive, direction and supervision, and more detailed reviews by more experienced and suitably competent members of the ET; and
 - Other relevant factors that may impact the required involvement of the EP.
69. Further, the EP's involvement in the engagement will also be informed by the EP's understanding of the engagement (see proposed new Paragraph 8A in **Agenda Item 5-B**), as well as risks to quality that have been identified and considered in addressing the requirements of ISA 220.
70. Additionally, examples in the application material of differing circumstances will help clarify how to appropriately 'flex' the nature, timing and extent of direction, supervision and review in order to have a basis for concluding that the level of involvement of the EP has been sufficient. For example, different scenarios could be presented, such as:
- An audit of a small, non-complex entity with limited risks—where the nature, timing and extent of active involvement by the EP in the day-to-day oversight of the engagement might be on the lower end of the spectrum (e.g., less frequent interactions with the team as they carry out further audit procedures and higher level reviews of the audit documentation), with relatively more responsibility for direction and supervision of team members being assigned to another suitably experienced and competent member of the ET such as the engagement manager (e.g., daily interactions with team members, on-the-job training and mentoring, and more detailed reviews).
 - A new engagement for the firm for an entity that operates in an industry with complex financial reporting issues and the ET is comprised primarily of new staff—where the necessary involvement the EP would need to be on the higher end of the spectrum (e.g., more involvement in the day-to-day oversight of the engagement, including more frequent and more in-person interactions with the team, and more extensive and more detailed reviews being performed by the EP).
 - An engagement where some of the audit procedures are undertaken at an ADM—including demonstrating the factors that would need to be taken into account when determining the appropriate nature, timing and extent of the direction, supervision and review when the ET is distributed, i.e., to have a basis for concluding that the involvement of the EP was sufficient.
71. In developing this application material, the Task Force also believes that including specific examples of situations where there are ET members or others involved in the audit who are located in different geographical locations to the EP or when the team operates on a virtual basis (e.g., ADMs, situations where the EP is not located where the majority of the audit work is performed, or where ET members are from network firms or from firms that are not part of the same network) will also help auditors understand how to apply the requirements in different circumstances. The Task Force also notes that these revised requirements will form the foundation for future proposed changes to ISA 600, and will be responsive to calls to further clarify the application of the requirements of ISA 220 to audits of group financial statements.

72. The Task Force also suggests that the application material could build on the concepts in *A Framework for Audit Quality: Key Elements that Create an Environment for Audit Quality*¹⁹ relating to the active involvement of the EP in the planning, supervision and review, as appropriate.
73. With regard to paragraph 17 of extant ISA 220 that addresses reviews of audit documentation by the EP, the Task Force discussed how to emphasize the objective of reviews and how this can be achieved in different circumstances in order to effectively manage the risks to quality at the engagement level. In addition to providing application material of differing circumstances that will help clarify how to appropriately ‘flex’ the nature, timing and extent of direction, supervision and review described above, in its discussions the Task Force agreed that elevating the application material in paragraph A18 of extant ISA 220 to the requirement in paragraph 17 would help clarify the minimum aspects that the EP is required to review. Paragraph A18 identifies certain areas where the EP should perform timely reviews in order to allow significant matters to be resolved on a timely basis and to the EP’s satisfaction. The Task Force believes that additional clarity on where the EP should focus his or her attention would be important and assist the EP in determining whether sufficient appropriate audit evidence has been obtained to support the conclusions reached and the issuance of the auditor’s report in the circumstances. The Task Force also has the view that no further prescription is required as the approach to reviews would and should be dependent on the specific circumstances of, and the risks to quality for, each engagement.
74. The Task Force also discussed including additional application material on other suggested areas where the EP may want to focus their reviews, as well as language that encourages the EP to, at a minimum, review the areas required to be reviewed by the EQC reviewer, if there is an EQC reviewer. The Task Force is also of the view that information required to be reviewed by the ECQ reviewer would warrant review by the EP. The Task Force will continue to monitor changes to ISQC 1 to determine the necessary consequential changes to be made in ISA 220, if any, as further consideration is given by the QCTF to EQC reviews.

Matters for IAASB Consideration:

10. The IAASB is asked for its views on the matters set out in paragraphs 65–74 above relating to the direction, supervision, performance and review. Specifically:
- (a) Are the factors describing the impact on the nature, timing and extent of the direction, supervision and review of the engagement described in paragraph 68 helpful? Are there any other factors that would influence the involvement of the EP that should be described?
 - (b) Would application material, such as that described in paragraph 70, be sufficient to demonstrate how the nature, timing and extent of the EP’s involvement in the audit is ‘flexed’ based on complexity of the entity and the underlying risks to quality? Are there other examples of different circumstances that should be included?
 - (c) Is it clear how addressing the risks to quality described in the standard help the EP determine the nature, timing and extent of the direction, supervision and review that is appropriate for the engagement (i.e., are revised paragraphs 15 and new 15A in **Agenda Item 5-B** sufficiently clear)?

¹⁹ Appendix 2, paragraphs 50–55 of the Framework sets out the key attributes for the EP at the engagement level, including that the EP is actively involved in risk assessment, planning, supervising, and reviewing the work performed.

- | |
|---|
| (d) Should additional application guidance be developed regarding the areas of focus for the EP in undertaking review activities, and if so, what should the areas of focus be? |
|---|

Consultation and Differences of Opinion

75. These sections include proposed revisions to illustrate how the four-step approach for quality management could be introduced. Additional changes will likely be necessary and will be considered by the Task Force as the QCTF progresses the revisions to these elements in ISQC 1.
76. With regard to the EP's responsibility relating to consultation on difficult and contentious matters, the Task Force is of the view that the relevant aspects of the existing requirement should be retained in the proposed revision to maintain the existing robustness relating to consultation.

EQC Reviews

77. **Agenda Item 2-A** sets out the QCTF's views on a separate standard addressing EQC reviews, which would have a consequential impact on ISA 220 that would need to be considered by the Task Force. Further, it is the view of the Task Force that the EP's responsibilities in relation to the EQC review (as outlined in paragraph 19 of extant ISA 220) should remain in ISA 220 if the requirements relating to the performance of the EQC review are moved to a separate standard. The Task Force will also further consider the EP's responsibilities in light of proposed changes to the criteria for determining when an EQC review is required.

Monitoring

78. The QCTF are proposing that ISQC 1 be strengthened in this area, with the proposed changes including enhanced requirements for monitoring and remediation. The new draft proposed requirement includes, in determining the scope and frequency of the monitoring activities, that the firm take into consideration:
- (a) The design and implementation of the firm's system of quality management;
 - (b) Changes in factors that have impacted the firm's system of quality management;
 - (c) The results of previous monitoring activities and remedial actions, including whether the previous monitoring activities continue to be relevant in evaluating the firm's system of quality management; and
 - (d) Other information that may suggest deficiencies exist in the firm's system of quality management, including information from external inspections, which may indicate the need for the firm to conduct monitoring activities.
79. The ISA 220 Task Force will further consider how the implications of the amendments to monitoring and remediation in ISQC 1 once the IAASB has provided its views on the changes being proposed by the QCTF.

Overall Stand-back before Concluding that Quality has been Effectively Managed at the Engagement Level

80. ISA 220 sets out the core elements required to be addressed in managing quality at the engagement level (see paragraphs 23–26 above). As noted in those paragraphs, the Task Force debated whether

there could be something else other than the core elements that would be relevant to managing quality at the engagement level and that would therefore need to be addressed in ISA 220. As discussed in paragraph 27 within Section C above, the Task Force agreed that these core elements were complete. The Task Force is therefore of the view that appropriate consideration of the requirements of this ISA as they relate to the core elements would provide the basis for the EP's conclusion as to whether quality has been managed effectively at the engagement level, i.e., that the management of quality at the engagement level has been effective in meeting the objective of the standard. The Task Force is, however, also of the view that it would be appropriate for the EP to evaluate, at the end of the engagement, how the requirements of the ISA have been addressed, and in particular whether there are any unaddressed risks to quality (e.g., as a result of new or changed facts and circumstances) that could impact audit quality, and for which additional actions could be necessary.

81. In addition, unexpected changes may arise during the audit that may necessitate the need to develop a response to a “new” risk to quality that may not have been identified through the other discrete requirements within ISA 220 (e.g., acceptance and continuance, determination of engagement resources, etc.). For example, should information come to the attention of the EP during the audit related to poor inspections findings in relation to a component auditor, the EP may need to adjust the approach to directing and supervising the work of that component auditor, including the nature, timing, and frequency of communications and nature and extent of reviews of their work. This risk to audit quality may not have been identified when the EP initially determined and selected the engagement resources, but given that it represents a risk to quality that has now been identified additional actions will need to be undertaken. The Task Force therefore proposes a stand-back requirement to be included in ISA 220 (see new paragraph 23A in **Agenda Item 5-B**).
82. This stand-back approach is consistent with the approach taken in other ISAs that seeks to achieve a quality audit. For example, paragraph 25 of ISA 330, in the section on “Evaluating the Sufficiency and Appropriateness of Audit Evidence,” states that “Based on the audit procedures performed and the audit evidence obtained, the auditor shall evaluate before the conclusion of the audit whether the assessments of the risks of material misstatement at the assertion level remain appropriate.” The Task Force also believes that including such a stand-back requirement would also assist in supporting the exercise of professional skepticism by the EP and other members of the ET.
83. The Task Force believes that this stand-back concept would be best applied in ISA 220 by requiring the EP to consider, before the completion of the audit and prior to forming a conclusion on the financial statements, whether the risks to quality have been appropriately addressed. The Task Force proposes that the requirement be supported by application material to explain that although this requirement is performed at the end of the engagement, it is not meant to preclude the EP from taking actions throughout the course of the engagement should other risks to quality arise while performing each of the discrete requirements in this standard. The Task Force also notes that a conforming amendment to ISA 700 (Revised),²⁰ paragraph 11 might be appropriate, i.e., to include consideration of “the engagement partner’s conclusion that quality has been effectively managed at the engagement level (ISA 220)” as part of the overall stand-back before forming an opinion on the financial statements.

²⁰ ISA 700 (Revised), *Forming an Opinion and Reporting on Financial Statements*

Matter for IAASB Consideration:

11. The IAASB is asked for its views on the matters set out in paragraphs 80–83 above relating to a new requirement for an overall stand-back before concluding that quality has been effectively managed and achieved at the engagement level.

Other Elements of ISA 220

Definitions

84. No changes were presented for the December 2016 IAASB meeting to any of the definitions within ISA 220. At the IAASB meeting, Board members highlighted that these definitions were consistent with the same definitions in the IESBA Code. The Board therefore noted that caution should be exercised in considering changes, and that collaboration with the IESBA would be important if any changes were believed to be necessary.
85. However, as it relates to the definition of EQC reviewer, the QCTF is currently considering changes to the definition as well as changes relating to the role and responsibilities of the EQC Reviewer – any changes, if any, made to the definition in ISQC 1 will therefore need to be replicated in ISA 220 once finalized.
86. In addition, QCTF is considering a new definition of “Quality Risk”. If supported by the Board, this definition would likely need to also be included within ISA 220, potentially amended for specific application in the context of an audit engagement. The QCTF’s discussion of the proposed definition in **Agenda Item 2-A** notes the need for the definition to be further considered in conjunction with the ISA 220 Task Force as it is also relevant to the concepts in ISA 220. The proposed definition included within **Agenda Item 2-B** is as follows:

Quality Risk – A risk that, individually or in combination, could reasonably have an adverse impact on the firm’s ability to achieve its quality objectives.

87. Although the Task Force proposes no further revisions to any definitions in ISA 220 at this stage; however this may change based on further discussions of the QCTF and the Task Force and Board input. If changes to the definitions are ultimately contemplated, the Task Force acknowledges that any changes will need to be made in careful coordination with the IESBA. Consistent with Board feedback, the Task Force also continues to have the view that additional application material supporting the definitions as described in Agenda Item 8-B of the December 2016 IAASB meeting agenda materials (and as set out below) will be helpful in illustrating how the definitions might be applied to different and evolving situations.

Application Material

88. In relation to the definitions, the following application material could be considered (either to the definitions or in support of specific requirements in the standard):
- (a) Engagement team – Providing examples of different types of ETs, including examples of individuals who would form part of the ET, including:
- Individuals working on the engagement who are situated at or part of ADMs – through describing various scenarios of such arrangements as well as demonstrating the considerations for ETs to apply in determining whether to use an ADM and how use of

an ADM should be addressed in designing appropriate direction, supervision and review (see paragraph 94 below).

- Individuals from a network firm that are involved in the audit, but who do not meet the definition of component auditors in ISA 600 (including addressing the impact on the direction, supervision and review by the EP).
 - Other examples where individuals may be working on an engagement that is not a traditional structure (i.e., not all working from the same location, engaged from other firms not included in the network).
- (b) EQC Reviewer – Clarify that the EQC reviewer is not considered a member of the ET and that the work of the EQC reviewer is not considered audit procedures.
- (c) **Agenda Item 4-A** sets out the discussion regarding networks. At this stage it is not contemplated that there will need to be a change to the definition but discussions of that paper may highlight the need for additional application material (either in ISA 220 or in ISQC 1, or possibly both) to highlight the different types of network arrangements that exist, and how network-level policies or procedures may be relevant to, and should be considered as part of managing quality at the firm and engagement level.

Additional Topics Discussed by the Task Force

ADMs

89. Within ISA 220 specifically, the topic of ADMs has become more relevant because of the growing use of centralized resources by ETs and the various ways that firm and ET structures are evolving. ADMs may be designed or intended to enhance audit quality, but may also give rise to new or different risks to quality at the engagement level. In particular, considerations related to ADMs are important for requirements addressing information and communication, determination of engagement resources, and direction, supervision, and review. This section of the Issues paper addresses matters related to ADMs that have been discussed by the Task Force. Certain matters are also addressed in the proposals for additional application guidance in the rest of this paper and in the proposed revisions to ISA 220 included in **Agenda Item 5-B**.
90. The ITC used the phrase “ADMs” to cover terms such as “firm shared service centers,” “centers of excellence,” “on-shoring,” “offshoring,” or “outsourcing”—essentially capturing how firms are reorganizing their structures and ETs, often in order to perform high quality audits at a reasonable cost. Respondents to the ITC supported actions to address issues around ADMs and other similar situations where other auditors are used. In considering the most appropriate actions, the Task Force agreed that additional application material is needed to help clarify that the definition of ET incorporates all those individuals who are under the direction, supervision and review of the EP (with the exception of those specifically covered by other ISAs as noted).
91. To help demonstrate who is considered to be part of the ET, examples of various scenarios could be provided as application material to the definition of ET to illustrate where other auditors, who are not in the same place as the ET, form part of the ET. The Task Force is of the view that this approach would help auditors to distinguish who is part of the ET without specifically defining the concept “ADM,” which would be difficult due to the wide-ranging circumstances to which the term may apply.

92. To that end, the Task Force discussed several examples of how other auditors at ADMs are currently being used by ETs including:
- (a) At the planning stage, procedures to set up current year work papers, such as roll forward of prior year schedules, set up of analytics, trial balance and population of lead schedules and summaries of various reports and minutes;
 - (b) Substantive procedures that are “objective based” in areas such as cash (confirmations), inventory, accounts payable, accounts receivable, revenue, debt and plant property and equipment. Such substantive procedures could include testing the mathematical accuracy of a population, recalculations, checking reconciliations, verifying data in a population and external confirmation and data requests;
 - (c) At the completion stage, procedures could include financial statement tie out, preparation of cash flows, performing disclosure checklists; and
 - (d) Other areas included providing assistance with testing information technology general controls, journal entry testing, review of service organization reports to identify follow-up items, and quality checklists.
93. The Task Force believes that including examples in the application material describing the activities of individuals involved in the engagement at ADM’s may help clarify that these individuals are part of the ET, and therefore that the responsibilities of the ET members also applies to these individuals (i.e., separate requirements addressing individuals at ADMs is not needed). Such examples could also incorporate who/what is considered to be an ADM—signaling to ETs that a broad range of scenarios may be included in the definition of ET:
- Audit-related activities are outsourced to individuals that are not located within the local ET’s jurisdiction;
 - Audit-related activities are outsourced to individuals that are located within the same jurisdiction, but not in the same location, as the local ET; and
 - Audit-related activities are outsourced to individuals not under the auditing firm’s system of quality management (i.e., a third party).
94. Notwithstanding individuals situated at ADMs are part of the ET, there are also special considerations about the appropriate level of direction and supervision of the individuals at the ADMs, and review of the procedures performed when ADM arrangements exist. The Task Force is of the view that developing application material to illustrate what these considerations could be may also help embed the quality management principles by illustrating the ‘flexing’ of what needs to be done based on the circumstances. Identifying characteristics that would impact the auditor’s assessment of the timing, nature and extent of direction, supervision and review would also allow changing circumstances to be addressed as these arrangements continue to evolve. Relevant considerations that would impact the nature, timing and extent of the EP’s direction, supervision and review could include:
- (a) Risk, complexity and level of judgment required to perform the procedure(s) performed at the ADM;
 - (b) Restrictions arising from laws and regulations (e.g., confidentiality);

- (c) Applicable firm policies or procedures for quality management that are relevant to the ADM or centralized location;
- (d) Previous experience with the ADM or centralized location, as well as consideration of the results of any monitoring and remediation activities relating to that location; and
- (e) Competence of the individuals at the ADM.

These characteristics could be presented in the application material to help the EP determine the timing, nature and extent of their direction, supervision and review. The examples could also be developed to show the impact of different circumstances.

E. Way Forward

- 95. The Task Force will continue to develop the changes to ISA 220 based on feedback from the Board, and other planned outreach in the second half of 2017, with the objective of being able to present a first read of an exposure draft to the IAASB in December 2017. The Task Force will also continue to monitor the changes being made to ISQC 1 to ensure consistency of the changes being made in ISA 220 where appropriate.
- 96. The Task Force also continues to consider issues around experts or individuals with specialized skills who are considered part of the ET, and whether external experts engaged by the auditor should be part of the ET. These matters will be further discussed by the Task Force and recommendations, if any, discussed with the Board at a future Board meeting.

Matter for IAASB Consideration:

- 12. Are there any other matters that the Task Force should consider in progressing the revision to ISA 220?

Appendix A

Approved Minutes – December 2016 IAASB Meeting

Quality Control – ISA 220

Ms. Zietsman presented the Board with the Crossover Working Group's (Crossover WG's) initial views on possible revisions to ISA 220 from the responses to the ITC as set out in **Agenda Items 8-A and 8-B**. The possible revisions included suggested enhancements to many of the extant requirements and application guidance in ISA 220, the introduction of possible new requirements to embed quality management principles at the engagement level and to address communications among members of the engagement team and others involved in the audit.

There was general agreement from the Board on the direction of the proposed enhancements put forward by the Crossover WG, with some areas for further consideration by the Task Force noted variously by Board members, including:

- Although supporting linking the objective of the auditor to managing quality of the audit, it was noted that more clarity about how this would be operationalized in ISA 220 is required (in particular the interaction between a risk assessment for these purposes (i.e. risks to quality) versus the assessment of the risks of material misstatement as required by ISA 315 (Revised));
- Support for clarifying the engagement partner's (EP) overall responsibility and accountability for audit quality at the engagement level, while still allowing the EP the flexibility to assign certain responsibilities to other members of the engagement team;
- Further consideration of situations where the signing partner is different from the EP who was responsible for the direction supervision, and review of the work performed as a part of the audit;
- The need for appropriate coordination with the IESBA relating to considerations around the definitions of EP, engagement team, and network firms;
- Support for a new requirement related to strengthening two-way communication among the members of the engagement team and those involved in the audit; and
- Support for further consideration of how firms in networks interact, especially as relates to quality control

PIOB OBSERVER REMARKS

Prof. Van Hulle encouraged the Task Force to further consider supervision of auditors where audit work has been outsourced (e.g., to other auditors), in particular as it relates to responsibilities for direction, supervision and review as well as communication.

WAY FORWARD

The Crossover WG will continue to progress possible changes to ISA 220 for discussion by the IAASB at future meetings, including further considering how to embed quality management principles at the engagement level.