

Agenda Item 3-B

Proposed Quality Management-related Conforming Amendments to the Code

(Mark-up from ED)

SECTION 120

THE CONCEPTUAL FRAMEWORK

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Considerations for Audits, Reviews and Other Assurance Engagements

120.15 A3 Conditions, policies and procedures described in paragraphs 120.6 A1 and 120.8 A2 that might assist in identifying and evaluating threats to compliance with the fundamental principles might also be factors relevant to identifying and evaluating threats to independence. In the context of audits, reviews and other assurance engagements, the existence of a system of quality management system designed, implemented and operated by a firm in accordance with the quality management standards issued by the IAASB is an example of such conditions, policies and procedures.

Commented [A1]: Refer to agenda item 3-A Section B to sight discussion on Task Force proposal.

Amendment proposed as the original wording might be read to suggest that the mere existence of a SOQM is an example of "conditions, policies and procedures." Instead, it is the actual design, implementation and operation of the SOQM that represent the "conditions, policies and procedures."

SECTION 300

APPLYING THE CONCEPTUAL FRAMEWORK – PROFESSIONAL ACCOUNTANTS IN PUBLIC PRACTICE

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The Firm and its Operating Environment

300.7 A5 A professional accountant's evaluation of the level of a threat might be impacted by the work environment within the accountant's firm and its operating environment. For example:

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- The engagement partner having authority within the firm for decisions concerning compliance with the fundamental principles, including any decisions about accepting or providing services to a client.

Commented [A2]: Refer to agenda item 3-A Section B to sight discussion on Task Force proposal

SECTION 320

PROFESSIONAL APPOINTMENTS

Client and Engagement Acceptance

General

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320.3 A3 A self-interest threat to compliance with the principle of professional competence and due care is created if the engagement team does not possess, or cannot acquire, the competencies to perform the professional services.

320.3 A4 Factors that are relevant in evaluating the level of such a threat include:

- An appropriate understanding of:
 - The nature of the client's business;
 - The complexity of its operations;
 - The requirements of the engagement; and
 - The purpose, nature and scope of the work to be performed.
- Knowledge of relevant industries or subject matter.
- Experience with relevant regulatory or reporting requirements.
- Whether the firm has implemented policies ~~or~~ and procedures, as part of a system of quality management in accordance with quality management standards such as ISQM 1, that respond to quality risks relating to the firm's ability to perform the engagement in accordance with professional standards and applicable legal and regulatory requirements.

Commented [A3]: Refer to agenda item 3-C comment #11.

The Task Force is proposing a change made to avoid inconsistency with the rest of the Code which refers to 'policies and procedures'. Based on discussion with IAASB staff, the wording in ISQM 1 was changed to 'policies or procedures' to allow for greater scalability as many SMPs may have procedures but not necessarily policies.

Commented [A4]: Refer to agenda item 3-C comment #10.

Task Force proposal to respond to a respondent's comment not to presume that ISQM 1 is adopted and that not implementing policies or procedures "in accordance with ISQM 1" could increase the level of threats.

SECTION 330

FEES AND OTHER TYPES OF REMUNERATION

Contingent Fees

330.4 A1 Contingent fees are used for certain types of non-assurance services. However, contingent fees might create threats to compliance with the fundamental principles, particularly a self-interest threat to compliance with the principle of objectivity, in certain circumstances.

330.4 A2 Factors that are relevant in evaluating the level of such threats include:

- The nature of the engagement.
- The range of possible fee amounts.
- The basis for determining the fee.
- Disclosure to intended users of the work performed by the professional accountant and the basis of remuneration.

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- ~~Whether the firm has implemented policies or procedures, as part of a system of quality management in accordance with ISQM 1, that address threats to compliance with the fundamental principles. Quality management policies and procedures.~~
- Whether an independent third party is to review the outcome or result of the transaction.
- Whether the level of the fee is set by an independent third party such as a regulatory body.

Commented [A5]: Refer to agenda item 3-C, comment #11.

The fifth bullet point of the extant Code refers generally to *'Quality control policies and procedures'* as a factor relevant in evaluating threats created by contingent fees. The proposed amendment inadvertently restricted this provision to policies or procedures under ISQM 1 relating to addressing threats to the fundamental principles. In addition, the amendment tied this provision to ISQM 1 whereas Section 330 also covers engagements that are not within the scope of ISQM 1. Accordingly, the extant wording has been reinstated but referring to quality management instead of quality control.

The difference between this bullet point and the last bullet point of paragraph 320.3 A4 reflects the difference between these two bullet points in the extant Code. Extant paragraph 320.3 A4 refers to "quality control policies and procedures designed to provide reasonable assurance that engagements are accepted only when they can be performed competently," i.e., it is focused more narrowly on the fundamental principle of professional competence and due care. In contrast, as noted above, paragraph 330.4 A2 refers much more broadly to "quality control policies and procedures" in context of contingent fees.

INTERNATIONAL INDEPENDENCE STANDARDS (PARTS 4A AND 4B)

PART 4A – INDEPENDENCE FOR AUDIT AND REVIEW ENGAGEMENTS

SECTION 400

APPLYING THE CONCEPTUAL FRAMEWORK TO INDEPENDENCE FOR AUDIT AND REVIEW ENGAGEMENTS

Introduction

General

400.4 ISQM 1 requires a firm to design, implement and operate a system of quality management for audits or reviews of financial statements performed by the firm. As part of this system of quality management, ISQM 1 requires the firm to establish quality objectives that address the fulfillment of responsibilities in accordance with relevant ethical requirements, including those related to independence. Under ISQM 1, relevant ethical requirements are those related to the firm, its personnel and, when applicable, others subject to the independence requirements to which the firm and the firm's engagements are subject ~~(including the network, network firms, individuals in the network or network firms, or service providers)~~. ISAs and ISREs establish responsibilities for engagement partners and engagement teams at the level of the engagement for audits and reviews, respectively. The allocation of responsibilities within a firm will depend on its size, structure and organization. Many of the provisions of this Part do not prescribe the specific responsibility of individuals within the firm for actions related to independence, instead referring to "firm" for ease of reference. A firm assigns operational responsibility for compliance with independence requirements to an individual(s) in accordance with ISQM 1. In addition, an individual professional accountant remains responsible for compliance with any provisions that apply to that accountant's activities, interests or relationships.

Commented [A6]: Refer to agenda item 3-C, comment #12.

Task Force proposal to respond to respondents' comments regarding the concept of "service providers," which is not defined in the extant Code but in ISQM 1 and is being addressed under the Engagement Team – Group Audits Independence (ET-GA) project. The Task Force recommends that this change be introduced through a conforming amendment from the ET-GA project.

Network Firms

R400.53 When determining whether a network is created by a larger structure of firms and other entities, a firm shall conclude that a network exists when such a larger structure is aimed at co-operation and:

- (a) It is clearly aimed at profit or cost sharing among the entities within the structure. (Ref: Para. 400.53 A2);
- (b) The entities within the structure share common ownership, control or management. (Ref: Para. 400.53 A3);
- (c) The entities within the structure share common quality management policies ~~and~~ procedures. (Ref: Para. 400.53 A4);
- (d) The entities within the structure share a common business strategy. (Ref: Para. 400.53 A5);
- (e) The entities within the structure share the use of a common brand name. (Ref: Para. 400.53 A6, 400.53 A7); or

Commented [A7]: Refer to agenda item 3-C comment #11.

The Task Force is proposing a change made to avoid inconsistency with the rest of the Code which refers to 'policies and procedures'. Based on discussion with IAASB staff, the wording in ISQM 1 was changed to 'policies or procedures' to allow for greater scalability as many SMPs may have procedures but not necessarily policies.

- (f) The entities within the structure share a significant part of professional resources. (Ref: Para 400.53 A8, 400.53 A9).

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400.53 A4 Common quality management policies **or** procedures are those designed, implemented and operated across the larger structure. (Ref: Para. R400.53(c)).

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Breach of an Independence Provision for Audit and Review Engagements

When a Firm Identifies a Breach

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R400.80 If a firm concludes that a breach of a requirement in this Part has occurred, the firm shall:

- (a) End, suspend or eliminate the interest or relationship that created the breach and address the consequences of the breach;
- (b) Consider whether any legal or regulatory requirements apply to the breach and, if so:
 - (i) Comply with those requirements; and
 - (ii) Consider reporting the breach to a professional or regulatory body or oversight authority if such reporting is common practice or expected in the relevant jurisdiction;
- (c) Promptly communicate the breach in accordance with its policies and procedures to:
 - (i) The engagement partner;
 - (ii) **These individuals(s) with operational responsibility for the policies and procedures relating to compliance with independence requirements;**
 - (iii) Other relevant personnel in the firm and, where appropriate, the network; and
 - (iv) Those subject to the independence requirements in Part 4A who need to take appropriate action;
- (d) Evaluate the significance of the breach and its impact on the firm's objectivity and ability to issue an audit report; and
- (e) Depending on the significance of the breach, determine:
 - (i) Whether to end the audit engagement; or
 - (ii) Whether it is possible to take action that satisfactorily addresses the consequences of the breach and whether such action can be taken and is appropriate in the circumstances.

In making this determination, the firm shall exercise professional judgment and take into account whether a reasonable and informed third party would be likely to conclude that the firm's objectivity would be compromised, and therefore, the firm would be unable to issue an audit report.

Commented [A8]: Refer to agenda item 3-C comment #11.

The Task Force is proposing a change made to avoid inconsistency with the rest of the Code which refers to 'policies and procedures'. Based on discussion with IAASB staff, the wording in ISQM 1 was changed to 'policies or procedures' to allow for greater scalability as many SMPs may have procedures but not necessarily policies.

Commented [A9]: Refer to agenda item 3-C, comment #5.

Task Force proposal to reflect suggestion from IRBA, i.e., to align with wording in ISQM 1, paragraph 20(c)(i).

Subparagraph (c)(ii) indicates the individual(s) to whom the communication of the breach is to be made. It does not set any requirement or expectation as to how that individual(s) discharges their responsibilities. This is addressed by ISQM 1 as part of the firm's system of quality management. Any breach communicated will be dealt with in the context of how the system of quality management has been set up, including the processes and assignees that this individual(s) has designated to assist them in fulfilling their responsibility.

400.80 A1 A breach of a provision of this Part might occur despite the firm having a system of quality management designed to address ~~and maintain~~ independence ~~requirements~~. It might be necessary to end the audit engagement because of the breach.

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Mergers and Acquisitions

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R400.73 If, following the discussion set out in paragraph R400.72(b), those charged with governance request the firm to continue as the auditor, the firm shall do so only if:

- (a) The interest or relationship will be ended as soon as reasonably possible but no later than six months after the effective date of the merger or acquisition;
- (b) Any individual who has such an interest or relationship, including one that has arisen through performing a non-assurance service that would not be permitted by Section 600 and its subsections, will not be a member of the engagement team for the audit or the individual responsible for the engagement quality review; and
- (c) Transitional measures will be applied, as necessary, and discussed with those charged with governance.

400.73 A1 Examples of such transitional measures include:

- Having a professional accountant review the audit or non-assurance work as appropriate.
- Having a professional accountant, who is not a member of the firm expressing the opinion on the financial statements, perform a review that is consistent with the objective of an engagement quality review.
- Engaging another firm to evaluate the results of the non-assurance service or having another firm re-perform the non-assurance service to the extent necessary to enable the other firm to take responsibility for the service.

SECTION 410 (REVISED)

FEES

Requirements and Application Material

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410.4 A4 The conditions, policies and procedures described in paragraph 120.15 A3 (particularly ~~the existence of a~~ system of quality management ~~system~~ designed, implemented and operated by the firm in accordance with the quality management standards issued by the IAASB) might also impact the evaluation of whether the threats to independence are at an acceptable level.

Commented [A10]: Refer to agenda item 3-C, comment #14,

Task Force proposal to respond to a respondent's comment that the statement that the system of quality management is responsible for "maintaining" independence is inconsistent with ISQM 1.

Commented [A11]: Refer to agenda item 3-A Section B to sight discussion on Task Force proposal.

Amendment to conform to the change proposed to paragraph 120.15 A3.

SECTION 540

LONG ASSOCIATION OF PERSONNEL (INCLUDING PARTNER ROTATION) WITH AN AUDIT CLIENT

Requirements and Application Material

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Service in a combination of key audit partner roles

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R540.15 Subject to paragraph R540.16(a), if the individual acted in a combination of key audit partner roles and served as the key audit partner responsible for the engagement quality review for four or more cumulative years, the cooling-off period shall be three consecutive years.

[Note: Conforming amendments were made to paragraphs R540.5(b) and R540.12 to replace the terms "engagement quality control review" with "engagement quality review" as part of the finalization of the [EQR revisions](#).]

R540.16 If an individual has acted in a combination of engagement partner and engagement quality reviewer roles for four or more cumulative years during the time-on period, the cooling-off period shall:

- (a) As an exception to paragraph R540.15, be five consecutive years where the individual has been the engagement partner for three or more years; or
- (b) Be three consecutive years in the case of any other combination.

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PART 4B (REVISED) – INDEPENDENCE FOR ASSURANCE ENGAGEMENTS OTHER THAN AUDIT AND REVIEW ENGAGEMENTS

SECTION 900

APPLYING THE CONCEPTUAL FRAMEWORK TO INDEPENDENCE FOR ASSURANCE ENGAGEMENTS OTHER THAN AUDIT AND REVIEW ENGAGEMENTS

Introduction

General

900.3 ISQM 1 requires a firm to design, implement and operate a system of quality management for assurance engagements performed by the firm. As part of this system of quality management, ISQM 1 requires the firm to establish quality objectives that address the fulfillment of responsibilities in accordance with relevant ethical requirements, including those related to independence. Under ISQM 1, relevant ethical requirements are those related to the firm, its personnel and, when applicable, others subject to the independence requirements to which the firm and the firm's engagements are subject ~~(including the network, network firms, individuals in the network or network firms, or service providers)~~. In addition, ISAEs and ISAs establish responsibilities for engagement partners and engagement teams at the level of the engagement. The allocation of responsibilities within a firm will depend on its size, structure and organization. Many of the provisions of Part 4B do not prescribe the specific responsibility of individuals within the firm for actions related to independence, instead referring to "firm" for ease of reference. A firm assigns operational responsibility for compliance with independence requirements to an individual(s) in accordance with ISQM 1. Additionally, an individual professional accountant remains responsible for compliance with any provisions that apply to that accountant's activities, interests or relationships.

Commented [A12]: To conform to paragraph 400.4.

GLOSSARY, INCLUDING LISTS OF ABBREVIATIONS

Engagement quality review	An objective evaluation of the significant judgments made by the engagement team and the conclusions reached thereon, performed by the engagement quality reviewer and completed on or before the date of the engagement report.
Engagement quality reviewer	A partner, other individual in the firm, or an external individual, appointed by the firm to perform the engagement quality review.
Key audit partner	The engagement partner, the individual responsible for the engagement quality review, and other audit partners, if any, on the engagement team who make key decisions or judgments on significant matters with respect to the audit of the financial statements on which the firm will express an opinion. Depending upon the circumstances and the role of the individuals on the audit, "other audit partners" might include, for example, audit partners responsible for significant subsidiaries or divisions.
Network	A larger structure: (a) That is aimed at co-operation; and (b) That is clearly aimed at profit or cost sharing or shares common ownership, control or management, common quality management policies <u>and/or</u> procedures, common business strategy, the use of a common brand-name, or a significant part of professional resources.

Commented [A13]: Refer to agenda item 3-C comment #11.

The Task Force is proposing a change made to avoid inconsistency with the rest of the Code which refers to 'policies and procedures'. Based on discussion with IAASB staff, the wording in ISQM 1 was changed to 'policies or procedures' to allow for greater scalability as many SMPs may have procedures but not necessarily policies.

LISTS OF ABBREVIATIONS AND STANDARDS REFERRED TO IN THE CODE

LIST OF ABBREVIATIONS

Abbreviation	Explanation
Assurance Framework	International Framework for Assurance Engagements
COSO	Committee of Sponsoring Organizations of the Treadway Commission
CoCo	Chartered Professional Accountants of Canada Criteria of Control
IAASB	International Auditing and Assurance Standards Board
IESBA	International Ethics Standards Board for Accountants
IFAC	International Federation of Accountants
ISAs	International Standards on Auditing
ISAEs	International Standards on Assurance Engagements
ISQMs	International Standards on Quality Management
ISREs	International Standards on Review Engagements

LIST OF STANDARDS REFERRED TO IN THE CODE

Standard	Full Title
ISA 320	Materiality In Planning and Performing an Audit
ISA 610 (Revised 2013)	Using the Work of Internal Auditors
ISAE 3000 (Revised)	Assurance Engagements Other than Audits or Reviews of Historical Financial Information
ISQM 1	Quality Management for Firms that Perform Audits or Reviews of Financial Statements, or Other Assurance or Related Services Engagements
ISQM 2	Engagement Quality Reviews
ISRE 2400 (Revised)	Engagements to Review Historical Financial Statements

