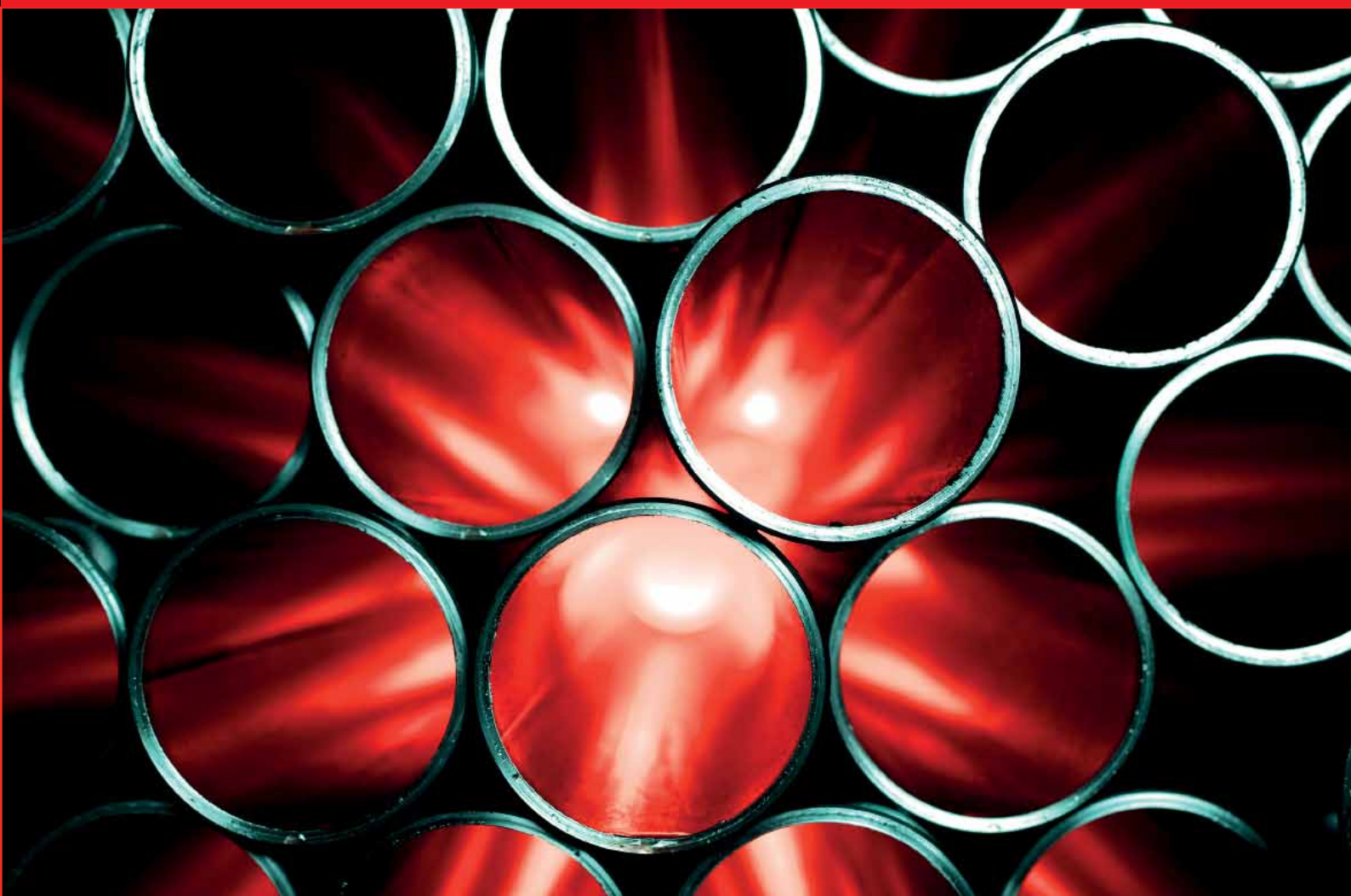




AUDIT &
ASSURANCE
FACULTY

QUALITY CONTROL IN THE AUDIT ENVIRONMENT

A practical guide for firms on the clarified ISQC (UK and Ireland) 1



The Audit and Assurance Faculty (the faculty) is a leading UK authority on external audit and other assurance activities. It is recognised nationally and internationally by members, professional bodies and others as a source of expertise on all audit issues. The faculty's membership includes internal and external auditors from a wide range of organisations and within practice, which enables it to speak on audit matters.

The faculty membership consists of nearly 8,000 members drawn from practising firms and organisations of all sizes from both the private and public sectors.

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FOREWORD

This publication is an updated version of the Audit and Assurance Faculty guide on quality control for audit firms first issued in May 2006. It takes into account recent developments, including the issue by the Auditing Practices Board (APB) in October 2009 of a clarified version of International Standard on Quality Control (UK and Ireland) 1 (ISQC (UK and Ireland) 1) *Quality control for firms that perform audits and reviews of financial statements, and other assurance and related services engagements*. This redrafted standard is effective for engagements relating to financial periods ending on or after 15 December 2010.

While audit practitioners are already familiar with the current ISQC (UK and Ireland) 1 requirements, and the new standard is 'redrafted' rather than 'revised', it is nevertheless important for auditors to understand and give careful consideration to the requirements in the new standard, as it does clarify the obligations imposed on them by eliminating ambiguity that might have existed in the previous version of the standard.

One matter that firms are likely to need to consider is establishing lines of communication (if they do not already exist) with external reviewers who may be called upon to perform reviews (see the sections on key areas 6 and 7). This might be a particular action point for sole practitioners and firms with a very small number of responsible individuals in the light of the requirement in paragraph 48 of ISQC (UK and Ireland) 1. This concerns the review of completed engagements which cannot be undertaken by the engagement partner, so increasing the likelihood that external reviewers will become more involved in performing these.

This publication concentrates on the ISQC (UK and Ireland) 1 requirements on quality control for firms rather than the International Standard on Auditing (ISA) (UK and Ireland) 220 requirements for individual audit engagements. It is intended to be of particular help to smaller firms, including sole practitioners and those firms with only one or two responsible individuals.

Seven key areas for firms to consider are identified with a section for each. Illustrative policies and procedures are given at the end of each section. It is hoped that the guide will help firms to determine what further practical measures they might need to take. However, reading this guidance is not a substitute for reading ISQC (UK and Ireland) 1.

Many firms use external providers for help on audit matters including quality control issues. However, it is important to emphasise that the firms have ultimate responsibility for the quality control policies and procedures they adopt and that any manuals or other documentation from external providers should be tailored to reflect the circumstances of each firm. It is highly likely that quality control guidance from external providers will only be of partial help to a firm when it determines issues such as its internal policies and leadership responsibilities. However, such guidance may help firms to formulate, focus on and document these issues.

ISQC (UK and Ireland) 1 should be read in the context of the APB's *Statement of Scope and Authority of APB Pronouncements* which was also revised and issued with the new clarified International Standards on Auditing (ISAs) (UK and Ireland) and ISQC (UK and Ireland) 1 in October 2009. Paragraph 1–1 of ISQC (UK and Ireland) 1 states that the standard not only applies to audit engagements but also to reporting in connection with investment circulars and providing other assurance services where they relate to activities that are reported in the public domain and are therefore in the public interest.

THE SEVEN KEY AREAS

A firm's objective under ISQC (UK and Ireland) 1 is to establish and maintain a system of quality control to provide it with reasonable assurance that:

- (a) the firm and its personnel comply with professional standards and applicable legal and regulatory requirements; and
- (b) reports issued by the firm or engagement partners are appropriate in the circumstances.

The faculty recommends that firms follow the guidance below to give them confidence that they fulfil this objective (references in brackets are to the paragraphs in the standard that outline the requirements for these areas):

1. **Document the operation of the quality control system** so that the firm complies with the relevant ISQC (UK and Ireland) 1 requirements (paragraphs 17, 57–59).
2. **Lead from the top** giving consistent messages on the importance of quality control (paragraphs 16(a), 18–19).
3. **Act ethically** in accordance with the relevant Standards and pronouncements (paragraphs 16(b), 20–25).
4. **Accept only those engagements where the firm is confident it can provide a service in compliance with requirements** with particular emphasis on integrity and competencies (paragraphs 16(c), 26–28).
5. **Recruit, develop and support capable and competent staff** giving due attention to the firm's human resources policies and procedures (paragraphs 16(d), 29–31).
6. **Deliver quality audits** that comply with law, regulations and standards, including consulting when needed and meeting requirements for engagement quality control review (paragraphs 16(e), 32–47).
7. **Monitor and seek continuous improvement of the firm's system of quality control** and carry out a periodic objective inspection of a selection of completed audit engagements (paragraphs 16(f), 48–56).

This publication covers and expands on each of these seven key areas in the next seven sections. Illustrative policies and procedures are provided at the end of each section for selected aspects of each key area, including some examples for sole practitioners. Others will be needed to cover other points of the key areas. If these examples are used by firms, they will need to be tailored to firms' specific circumstances.

1. DOCUMENTATION

Document the operation of the quality control system so that the firm complies with the relevant ISQC (UK and Ireland) 1 requirements (paragraphs 17, 57–59).

ISQC (UK and Ireland) 1 requires documentation evidencing the operation of each element of the quality control system. One practical option is to create an ISQC (UK and Ireland) 1 file documenting the various policies (what the firm wants to do) and procedures (how the firm intends to achieve its ends) used to meet the requirements of ISQC (UK and Ireland) 1. Prior to ISQC (UK and Ireland) 1 coming into effect, some of these might not have been documented or perceived as part of the system of quality control. Some firms might find it helpful to produce a document that maps each requirement of ISQC (UK and Ireland) 1 to the policies and procedures of the firm on a line-by-line basis. All firms need to consider whether their existing documentation is sufficient to meet the requirements of the clarified ISQC (UK and Ireland) 1.

ISQC (UK and Ireland) 1 requires firms to establish, maintain and document both policies and procedures in respect of the various areas included. The level of documentation needed will depend on the size of firm and need not be onerous. In fact, a number of the required procedures eg, on acceptance and continuance, are likely to be covered by a firm's standard audit documentation.

Put simply, a policy is a statement of intent. For example, a firm might establish a policy that audit engagements will only be accepted if the firm can meet the relevant independence requirements. A procedure is the means by which the firm seeks to ensure the related policy is achieved. In this example, an appropriate procedure might be the completion of an independence checklist and the review and authorisation of both the completed checklist and the acceptance decision by the ethics partner. An ISQC (UK and Ireland) 1 compliant system of quality control should have no policies that are not supported by appropriate procedures. Also, it is inefficient to have procedures that do not support any defined policies.

While firms may be performing most of the required quality control procedures, these may not always be adequately documented as required by ISQC (UK and Ireland) 1. It is important that these procedures are performed in response to documented policies and that those within the firm responsible for ISQC (UK and Ireland) 1 compliance ensure that appropriate policies are established and documented.

However, as stated above, complying with ISQC (UK and Ireland) 1 should not mean firms incur excessive costs writing and producing updated procedures manuals. Indeed ISQC (UK and Ireland) 1 and the clarified ISAs might provide firms with the opportunity to examine their practices and find efficiencies and appropriate ways to manage the risks they face.

Taking another example regarding acceptance and continuance of an audit engagement, the policy for the firm might be that it shall only undertake or continue an assignment if the criteria set out in paragraph 26 sections (a) to (c) of ISQC (UK and Ireland) 1 have been met. (NB: firms can choose to set further criteria.) The procedure required to comply with the policy might be to complete the relevant section of the firm's standard audit package. The policy required may be somewhat more extensive for a large firm, and is likely to already be set out in a professional standards manual, for example. For a sole practitioner, the policy may not previously have been formally set out in writing even though it did exist, but to comply with ISQC (UK and Ireland) 1 this could be done succinctly eg, using a single sheet of paper or making a single statement within the ISQC 1 file might be sufficient.

This process would need to be repeated for each section of ISQC (UK and Ireland) 1. For a small firm it is envisaged that all the necessary policies could be set out in a short document, cross-referenced to where the documentation detailing or supporting the procedure can be found eg, engagement letter, standard audit package, employment contract etc. For a larger firm the policies and procedures are likely to be much more extensive but they still need documenting.

In documenting policies and procedures, it may be more effective and easier to use a series of concise bullet points aided by further explanation as and when necessary, or include reference to other available documentation (as suggested above) rather than pages of detailed procedures. This may include reference to on-line material, such as from the firm's intranet or available to the firm from a third party source. It may be sensible to download copies of such information and retain on file, and then periodically review the on-line content for changes from the firm's present procedures, to check that the procedures remain current. It may also be helpful to make reference to other sources of information within the firm, such as an employment manual or standard employment contract terms, audit procedures manual, ethics manual, etc, where this is appropriate.

The firm's documentation should be easily accessible to partners and staff involved in audit work. For example, this could be done through the use of a shared computer network drive or a procedures manual in the office. Audit partners and audit staff should be required to read and understand the procedures and changes to these, and this can include a requirement to sign to confirm that they have done this. They should be encouraged to use the material as appropriate.

Issues for small and medium-sized firms will be different to those in larger firms and often the policies and procedures for these firms can be simple and informal. Lines of communication are often short in smaller firms, and when new situations arise, the policies and procedures can be amended much more readily than in a larger practice, or multi-site firm where procedures may be centrally determined. The number of issues/areas to be covered and documented may therefore be greater for larger firms than for smaller firms.

Once a firm has developed its quality control policies and procedures, it is required to monitor compliance with those policies and procedures and to ensure that the relevant documentation is kept up to date, for example to reflect changes in the firm's procedures, personnel and audit and accountancy updates. Responsibility for doing this should be clearly assigned to a suitable person or persons within the firm.

The firm should be able to produce documented evidence of the operation of its quality control system. This will facilitate the monitoring element of quality control required by ISQC (UK and Ireland) 1 (see the section on key area 7). There are ICAEW Helpsheets which may help with this (see Appendix 4). Alternatively ISQC (UK and Ireland) 1 itself could be used and annotated to demonstrate where the relevant guidance can be found within the firm's own documentation.

Firms should also comply with the standard's requirements on engagement documentation – these are covered in the section on key area 6 (engagement performance).

ILLUSTRATIVE POLICIES AND PROCEDURES ON THE DOCUMENTATION OF THE FIRM'S QUALITY CONTROL SYSTEM

Documentation of all elements of the system of quality control

Policy: All elements of a system of quality control required to be documented by ISQC (UK and Ireland) 1 are documented.

Procedure: The firm has checklists, forms and the ISQC (UK and Ireland) 1 compliance file/handbook/manual to cover all the requirements.

Maintenance of the quality control system and awareness of partners and staff

Policy: Documentation of the firm's system of quality control is kept up to date, and all partners and members of staff are fully aware of the most recent version, including any newly introduced changes.

Procedures: The audit compliance partner (ACP) takes responsibility for ensuring that the firm publishes and stores policies and procedures electronically through the firm's intranet in order to make version control easier to achieve.

Specifically, the ACP will ensure that the firm:

- removes superseded policies and procedures from the firm's intranet;
- requires partners and staff to confirm in writing that they have updated hard-copy versions of the policies and procedures when updates are issued;
- clearly marks all quality control policies and procedures documents/files with their issue date and version number; and
- circulates control schedules detailing which quality control policies and procedures are current and implemented on a timely basis (eg, every time there is an addition or deletion, and also at regular intervals throughout the year independent of any changes).

FOR A SOLE PRACTITIONER

Documentation of the quality control system

Policy: The firm's system of quality control is appropriately documented to demonstrate compliance with ISQC (UK and Ireland) 1 and [name of sole practitioner] takes responsibility for ensuring this happens.

Procedures:

Either: The firm purchases and tailors a third-party quality control handbook/manual, issues this to staff and keeps it up to date.

Or: The firm maintains an ISQC (UK and Ireland) 1 file which includes policies to address the elements of a quality control system as set out in ISQC (UK and Ireland) 1 and how the firm will deliver them. This is kept up to date and the contents are clearly communicated to staff.

2. LEADERSHIP RESPONSIBILITIES

Lead from the top giving consistent messages on the importance of quality control (paragraphs 16(a), 18–19).

A key feature is that the firm's chief executive or senior partner or managing board (or equivalent) assumes ultimate responsibility for the firm's system of quality control.

The firm's leadership and the example it sets ('tone at the top') should significantly influence the internal culture of the firm. It will help to achieve the required culture if consistent messages on the importance of quality control are provided by way of internal communications and in meetings, training events and partner and staff appraisals and rewards.

For firms that use external sources for support in forming, documenting or performing their policies and procedures, it is important to emphasise that the managing partner (or equivalent) has to accept the ultimate responsibility for all aspects of the quality control system.

The firm's policies and procedures should help to promote an internal culture based on the recognition that quality is essential to performing engagements. It is suggested that firms place particular emphasis on ensuring that:

- commercial considerations never override the quality of performance;
- audit partners and staff are always sufficiently independent and approach audits with a mindset of professional scepticism;
- performance evaluation, compensation and promotion demonstrate the firm's commitment to quality; and
- sufficient appropriate resources are devoted to the development, documentation and support of the firm's quality control policies and procedures.

Operational responsibility for the firm's quality control systems may be assigned (eg, to a quality control partner or audit compliance partner) providing such personnel have the necessary experience and authority to assume that responsibility, but this does not affect the position regarding the ultimate responsibility for the system of quality control.

ILLUSTRATIVE POLICY AND PROCEDURE ON THE RESPONSIBILITY ASPECT OF LEADERSHIP

Leadership responsibilities – overall responsibility for the firm's audit work

Policy: The firm's management board bears ultimate responsibility for audit quality and promoting the importance of this to all partners and staff.

Procedure: At its meeting on [date inserted] the management board agreed to include this responsibility within their terms of reference and gave operational responsibility for this function to [name and title¹ inserted], who will report to the management board as required, and at least annually.

¹ For example, quality control partner.

FOR A SOLE PRACTITIONER

Responsibility for the firm's audit work

Policy: [Name of sole practitioner] has the final responsibility for audit quality and seeks to promote the importance of audit quality in all his/her actions connected with the firm's audit work.

Procedure: All changes to our audit procedures must be authorised by [name of sole practitioner] and any issues relating to audit quality should be drawn to [name of sole practitioner]'s attention immediately.

ILLUSTRATIVE POLICY AND PROCEDURE ON THE FIRM'S COMMITMENT TO ALLOCATING SUFFICIENT RESOURCES TO ENSURE QUALITY CONTROL

Allocation of resources to ensure quality control

Policy: The firm's management board allocates appropriate and sufficient resources to the development and documentation of its quality control policies and procedures.

Procedures:

The firm:

- delegates responsibility to the appropriate people to do this;
- establishes reasonable timetables and schedules for the production, review and issuing of relevant policies and procedures;
- provides training or reference material as appropriate;
- considers electronic publication and storage of such policies and procedures; and
- buys in a manual or handbook to form the basis and then tailors this as appropriate.

FOR A SOLE PRACTITIONER

Commitment to ensuring quality control

Policy: [Name of sole practitioner] allocates sufficient time and resources to the development and documentation of the firm's quality control policies and procedures.

Procedures:

- [Name of sole practitioner] takes responsibility for ensuring this happens;
- [Name of sole practitioner] liaises with [name of external provider which provides a quality control manual] and establishes reasonable timetables for the production and issue of relevant policies and procedures, tailored to the circumstances of the firm; and
- [Name of sole practitioner] liaises with [name of external provider] in order to provide appropriate training and reference material to staff.

3. ETHICAL REQUIREMENTS

Act ethically in accordance with the relevant Standards and pronouncements (paragraphs 16(b), 20–25).

Firms need reasonable assurance that they and their personnel comply with the relevant ethical requirements. ISQC (UK and Ireland) 1 gives particular guidance on the subject of independence. In the case of UK audits, firms can be confident that they will meet ISQC (UK and Ireland) 1's requirements if they comply with the APB's Ethical Standards for Auditors (ESs), including Provisions Available for Small Entities (ES-PASE) (www.frc.org.uk/apb/publications/ethical.cfm), and ethical standards and guidance issued by ICAEW (www.icaew.com/ethics). There are some exemptions and alternative provisions in the ES-PASE and these should be considered carefully where relevant.

The relationship between the ESs and the ES-PASE, and how to apply the latter, can be complex and challenging, particularly when accounting services are provided to clients.²

Firms might find it helpful to refer to the frequently asked questions on the APB Ethical Standards on the ethics section of the ICAEW website, available at www.icaew.com/ethicsadvice.

Firms should ensure that all audit partners and staff have appropriate and tailored training on ethical matters including the ESs and specific guidance that is available within the firm. Partners and staff ought to be aware of who or what to consult if they are uncertain on a particular matter. Specifically, there should be a policy and procedure on what staff should do if they have an ethical issue to resolve. Larger firms are likely to pay specific attention to the requirements that are relevant for listed audits and smaller firms might want to emphasise issues connected with the ES-PASE.

Paragraph 24 of ISQC (UK and Ireland) 1 requires an annual written statement on independence from all firm personnel required to be independent by relevant ethical requirements. It should be noted that this requirement is not restricted to partners and staff doing audit work but extends to all partners and staff doing work of any kind for audit clients. This requirement can most easily be met by using a standard form. However, partners and staff should be expected to report any new situation that could pose an independence problem on a timely basis.

ILLUSTRATIVE POLICY AND PROCEDURE ON THE NON-AUDIT SERVICES ASPECT OF ETHICAL REQUIREMENTS

Provision of non-audit services to audit clients

Policy: The firm only provides audit clients with non-audit services if they do not contravene the principles established by the APB Ethical Standards for Auditors and professional requirements.

Procedure³: All partners intending to carry out work for an audit client notify the audit engagement partner about the proposed non-audit service before such work commences so he/she can assess the overall impact of ethical requirements on whether the non-audit service can be undertaken in addition to the audit engagement.

² *Audit News* Issue 46 (available at www.icaew.com/auditnews) included a diagram to explain how the ES-PASE works.

³ There will be other procedures including those involving the firm's ethics partner so that audit engagement partners are aware of how to deal with situations where there could be an independence issue arising from the provision of a non-audit service.

FOR A SOLE PRACTITIONER

Compliance with ethical standards when engagements are accepted and continued

Policy: The firm only accepts or continues with audit engagements if they do not contravene the principles established by the APB Ethical Standards for Auditors and professional requirements.

Procedures: For each engagement accepted or continued, [name of sole practitioner] evaluates the impact of the relevant ethical standards and professional requirements on the engagements and takes such actions as required by those standards/requirements. This is documented as part of the client acceptance paperwork and kept on the file to demonstrate that the issues have been appropriately considered.

4. ACCEPTANCE AND CONTINUANCE

Accept only those engagements where the firm is confident it can provide a service in compliance with requirements with particular emphasis on integrity and competencies (paragraphs 16(c), 26–28).

Paragraph 26 of ISQC (UK and Ireland) 1 outlines the requirement for firms to have policies and procedures for the acceptance and continuance of client relationships and specific engagements. In summary, firms are required to consider and document as appropriate the following factors when accepting or continuing audit relationships and engagements:

- the integrity of the client;
- the firm's competence to perform the engagement; and
- whether compliance with ethical requirements can be achieved.

ISQC (UK and Ireland) 1 indicates the type of factors to consider, for example the reputation of the client's management and owners. A firm's knowledge of such matters will usually grow in the course of a continuing relationship with the client. While there is a requirement to obtain appropriate information to support a firm's decision to accept or continue an audit appointment, the requirement to document is where 'issues' may be identified and the firm decides to accept or continue the appointment. The reasons for accepting the appointment in such circumstances should be clearly documented.

Most firms are likely to adopt a checklist approach to this task and might use checklists provided by external sources as appropriate. However, firms ought to be alert to the dangers of completing a checklist in a mechanistic manner without giving the issues proper consideration. It is suggested that checklists give scope for the individuals completing them to insert comments where appropriate to expand on their conclusions.

As an alternative, some firms might consider developing an aide-mémoire covering the various issues to consider on acceptance and continuance and what should be documented. Standard forms often concentrate on integrity, money laundering and independence, and so it is important to properly incorporate the need for other considerations to be documented eg, on industry knowledge and specialist needs. Firms might consider whether to incorporate a procedure requiring second partner approval of the audit acceptance decision, at least for particular types of audit.

Some of the typical questions that firms should ask when considering acceptance and continuance are as follows:

- Is this a specialist area where specialist skills will be required?
- Are there complex accounting issues to consider eg, asset valuations, and if so, can we access the necessary expertise to deal with these?
- Are there going concern issues?
- Are there independence issues eg, relating to fee dependency on non-audit services?
- Have there been examples of fraud?
- Have we performed the necessary procedures relating to the money laundering regulations and are we comfortable with the results of those procedures?

- If this is a group audit, or part of a group, are there special considerations arising from ISA (UK and Ireland) 600 *Special considerations – audits of group financial statements (including the work of component auditors)*?⁴
- Is there likely to be a need for external consultation or to appoint an engagement quality control reviewer (see the section on key area 6), and if so, do we have appropriate people available to help us?

The answers to these questions will help the firm to assess the situation holistically and thereby take a decision on whether to accept the engagement. Issues that are identified will not necessarily preclude the firm from accepting the engagement, for example where there has been a significant fraud but appropriate action has been taken to deal with this.

As part of the acceptance and continuance exercise, firms have to consider whether partners and staff have the competencies to perform the engagements. Specifically, firms need to consider existing partner and staff profiles and competencies, and compare and, if possible, match these with the requirements of the existing and future client base. If gaps exist, appropriate action should be taken eg, enhancing competencies where required or ensuring that specialist help can be brought in as necessary. It is important for firms to document their judgements regarding these matters, for example why they believe they are still competent to do work which is becoming increasingly specialised.

Firms might find it useful to refer to the relevant ICAEW Helpsheets on engagement and disengagement (Helpsheets PAS 2/HS11 and 12, PAS2/HS13 and 24 – see Appendix 4). Engagement letters should be updated as appropriate. On cessation, all relevant matters should be considered which might be facilitated by having a proforma disengagement letter as well as a disengagement checklist.

ILLUSTRATIVE POLICY AND PROCEDURE ON THE ENGAGEMENT ACCEPTANCE ASPECT OF ACCEPTANCE AND CONTINUANCE

Acceptance and continuance – new and existing clients

Policy: The firm only accepts or continues an assignment if the firm has concluded that the client does not lack integrity, that the firm is competent and has the resources to perform the services required, and that the firm can comply with Ethical Standards.

Procedure⁵: The audit engagement partner undertakes appropriate investigations/assessments and completes the firm's client acceptance/continuance documentation before the acceptance/continuance decision and also completes the relevant sections of the firm's standard audit procedures during the course of the planning stage of the engagement. Where appropriate, [name] (the firm's ethics partner) or [name] (the individual with overall responsibility for quality control) is consulted before the final decision is taken.

FOR A SOLE PRACTITIONER

Acceptance and continuance – new and existing clients

Policy: The firm only accepts or continues an assignment if the firm has concluded that the client does not lack integrity, that the firm is competent and has the resources to perform the services required, and that the firm can comply with Ethical Standards.

Procedure⁶: [Name of sole practitioner] undertakes appropriate investigations/assessments and completes the firm's client acceptance/continuance documentation before the acceptance/continuance decision and also completes the relevant sections of the firm's standard audit procedures during the course of the planning stage of the engagement.

⁴ For more guidance on these issues, firms might refer to the faculty publication *Auditing in a Group Context: Practical Considerations for Auditors*.

⁵ NB: there will be other procedures on assigning a competent team and ensuring that the firm and the team have met independence and other ethical requirements.

⁶ As footnote 5 above.

5. HUMAN RESOURCES

Recruit, develop and support capable and competent staff giving due attention to the firm's human resources policies and procedures (paragraphs 16(d), 29–31).

ISQC (UK and Ireland) 1 requires firms to consider their human resources policies and procedures on issues such as recruitment, obtaining references, induction and career development, and assess the effectiveness of their performance evaluation and reward system. However, all of ISQC (UK and Ireland) 1's requirements could be regarded as sensible procedures for firms that wish to motivate and develop their staff and partners.

Firms should communicate their quality control policies and procedures to staff and partners and it is helpful to obtain feedback from them as to their views on quality control related matters so that changes can be made as appropriate.

Firms need policies and procedures to demonstrate:

- that there will be sufficient suitably qualified staff and partners with the competencies to cope with the number and complexity of audit assignments;
- that audit staff and partners will be trained and developed to ensure that they are sufficiently independent and approach audits with a mindset of professional scepticism;
- that the minimum standards required of audit staff and partners at the different levels of responsibility are in place within the firm, and that training arrangements are tailored to the needs of the firm and its clients; and
- more specifically, that the means of maintaining and keeping staff and partners up to date with developments in audit regulation and practice is established and formalised as part of a commitment to ensuring staff and partners comply with CPD requirements.

The firm should have suitable recruitment policies and should periodically evaluate capabilities and performance in an appropriate way, emphasising the importance of achieving high-quality audit work. For those firms with a small number of audits, it might be beneficial to designate audit 'specialist' staff. The appraisal system should provide for consideration of personal and career development issues for staff and partners and appraisal reviews ought to be formally documented. There should be a clear link between firms' appraisal processes and their training programmes and selection of audit team processes. Post-audit reviews and audit compliance reviews also play an important part in identifying personal development and training issues, and this again highlights the need for firms to have an integrated approach between their human resources and audit policies so that the training issues identified are properly recorded and acted upon, and the next year's audit planning gives proper consideration to these factors.

In summary, the engagement partner and staff assigned to audits via the audit planning process should have the appropriate experience and competencies necessary for that engagement. The firm needs to check that those thereby assigned to audits have the appropriate authority in accordance with the firm's procedures and the time to do the work, and the firm has to establish the policies and procedures to ensure that this is so. Written job descriptions and the budgeting of partner and staff time are likely to be part of this process. Annual statements of fit and proper status, independence and confidentiality should be received from all audit partners and staff. Contracts of employment need to be in line with the firm's requirements in this regard.

ILLUSTRATIVE POLICY AND PROCEDURE ON RECRUITMENT

Requirements relating to recruitment

Policy: The firm's recruitment programme is designed to provide the firm with appropriately qualified personnel possessing the right mix of skills and experience and the required personal characteristics, taking into account current client servicing commitments and anticipated future needs.

Selected procedures under the policy:

- Advertising for new recruits in professional publications.
- Retention of specialist recruitment services (eg, from an agency), selected by the firm based on their suitability to provide these services.
- Standardised prospective employee information forms.
- Transparent interview and call back processes.
- The obtaining of references.
- Viewing and following up on evidence of professional and educational qualifications.
- Assigning the responsibility for employment decisions to authorised persons.
- Monitoring the effectiveness of the recruitment programme.

FOR A SOLE PRACTITIONER

Requirements relating to recruitment

Policy: The firm's recruitment programme is designed to provide the firm with appropriately qualified personnel possessing the right mix of skills and experience and the required personal characteristics, taking into account current client servicing commitments and anticipated future needs.

Selected procedures under the policy:

- Advertising for new recruits in relevant local and professional publications.
- Recruitment support is provided by [name of external source], which is a reputable job agency for accountancy firms.
- Standardised prospective employee information forms.
- Transparent interview and call back processes.
- The obtaining of references.
- Viewing and following up on evidence of professional and educational qualifications.
- Periodically monitoring the effectiveness of the firm's recruitment processes.

ILLUSTRATIVE POLICY AND PROCEDURE ON STAFF REQUIREMENTS

Requirements on staff undertaking audit work

Policy: The firm will only deploy partners and staff to work on audits who have integrity and the relevant competencies.

One procedure under the policy⁷: The firm conducts an annual assessment of all partners and staff engaged on audit (including specialists) by the completion of questionnaires. We consider training needs as part of the performance review and appraisal process (including assessment of CPD) and decide on appropriate training programmes based on this.

FOR A SOLE PRACTITIONER

Requirements of persons undertaking audit work

Policy: The firm will only employ staff or commission external persons to work on audits who have integrity and the relevant competencies.

One procedure under the policy⁸: The firm conducts an annual assessment of all people employed or used on audit (including specialists) by the completion of questionnaires. We consider training needs for [name of sole practitioner] and staff as part of the performance review and appraisal process (including assessment of CPD) and decide on appropriate training programmes based on this.

⁷ There will be other human resources procedures which enable the policy to be delivered eg, on recruitment and how the firm decides that those assigned to the work will be appropriate.

⁸ As footnote 7 above.

6. ENGAGEMENT PERFORMANCE

Deliver quality audits that comply with law, regulations and standards, including consulting when needed and meeting requirements for engagement quality control review (paragraphs 16(e), 32–47).

Firms should establish procedures to enable audit engagements to be performed to the standards expected. Ordinarily, this will involve the use of manuals, checklists, and other tools. In particular, it is important for firms to recognise when consultation is needed.

Firms and the engagement teams carrying out audits need to comply with all the requirements of ISAs (UK and Ireland), including the requirements relating to risk and fraud. Experience has highlighted a number of operational issues of relevance to audit firms looking to achieve a high quality of audit work, including the need for:

- timely audit planning;
- appropriate and timely use of technical specialists on accounting and auditing matters; and
- effective post audit reviews which are linked to appraisal processes (see the section on key area 5) and which inform the planning of the next year's audit.

There are also a number of requirements relating to the engagement quality control review (EQCR⁹) – see below.

It is possible that firms will establish external relationships to help them with these matters. They should note that more than one external source may be required if conflicts of interest might arise eg, a contentious issue adviser might not be capable of also acting as engagement quality control reviewer. However, in practice these separate sources could be from the same external organisation.

CONSULTATION

In summary ISQC (UK and Ireland) 1 (paragraph 34) requires firms to establish policies and procedures to provide them with reasonable assurance that:

- consultation takes place on difficult or contentious issues;
- sufficient resources are available to enable the consultation to occur;
- the details of the consultation are documented and agreed with the consultee; and
- conclusions are implemented.

The need to consult a fellow professional may arise in a number of circumstances eg, interpretation of an accounting standard, considerations relating to going concern, adoption of specific accounting policies. Each firm will need to consider when consultation needs to take place and set this out within its documented policies. For example, in some circumstances the following situations may need consultation to help auditors to determine whether client policies are acceptable:

- the client proposes an accounting treatment or disclosure which could be a departure from an accounting or disclosure requirement;
- the client proposes to adopt an accounting policy that might be inconsistent with the industry norm;

⁹ Firms might refer to the EQCR as a second partner review or independent review but this could be misleading as these terms can also be used for other reviews which are not EQCRs.

- the client's treatment might be verging on aggressive earnings management;
- the complexity of the accounting is beyond that normally encountered by the firm;
- there are potentially problematic valuation issues, for example in determining fair value estimates;
- there are concerns regarding the client's going concern assessment; or
- the client might be unduly influenced by tax considerations in determining an accounting treatment.

The firm needs to put in place arrangements so that consultation is dealt with in a timely manner eg, if during the planning meeting the engagement partner becomes aware that there may be an issue, the potential person to be consulted should be put on notice that their advice may be required. The matter should then be dealt with and concluded upon as soon as practicable. The firm also needs to establish what information should be provided to the person being consulted. It is important that they are given sufficient background to the issue to be able to provide an informed opinion – unintentional cherry-picking of the information provided could lead to an incorrect conclusion. Useful information is likely to include the current year's draft financial statements, the prior year accounts and a written description of the issue together with copies of (or cross-referenced to) any relevant technical pronouncements/extracts of other companies' financial statements.

For multi-partner firms there should not be any significant hurdles to overcome in consulting with a fellow professional when necessary. For sole practitioners, firms with only one responsible individual or other small firms this can be more difficult. ICAEW Helpsheets might be of use to small firms in formalising consultation procedures (see Appendix 4). It is recommended that formal consultation relationships are established by all small firms so that these are in place when needed.

There can be a potential pitfall in the use of the engagement quality control review (EQCR) reviewer (see below) for consultation. (NB: this reviewer should not be confused with the audit compliance principal responsible for monitoring compliance with the Audit Regulations – see the section on key area 7.) While a level of consultation will inevitably occur to some extent on any assignment where an independent 'hot' review of an assignment is required, the nature of involvement should not be so extensive as to bring the independence and objectivity of the reviewer into question eg, involvement in decision making for the engagement team or in the performance of the audit. If this is the case it may be necessary to involve a third partner or appoint a new reviewer. The processes of consultation on individual issues should generally be separated from those of an engagement quality control review.

ENGAGEMENT QUALITY CONTROL REVIEWER

ISQC (UK and Ireland) 1 requires an engagement quality control review (EQCR) for all audits of listed entities and other entities as appropriate (determined by the firm's own criteria). The firm is required to have policies setting out the criteria to be considered when determining what audit engagements require such reviews in addition to those for listed entities. Criteria would normally include public interest, the nature of the engagement, and unusual circumstances or risks. Firms also need to ensure they comply with the requirements of ES 4 on fee dependency which mean that EQCRs will be needed in some circumstances.

Sole practitioners, firms with only one responsible individual or other small firms may only need to carry out EQCRs in exceptional circumstances and may use suitably qualified and experienced external persons or other firms to carry out these reviews where they are needed. It is helpful for these firms to identify the EQCR reviewer in advance where possible (see below). An external reviewer might be able to provide enhanced experience and knowledge and firms might therefore benefit from using the services of a 'fresh pair of eyes'. But firms taking this option do need to ensure that they are satisfied that the external person has the necessary skills and experience to undertake the role eg, regarding the key accounting issues.

The EQCR reviewer is not selected by the engagement partner. This is designed to safeguard the independence of the quality control process on individual audits. The appointment ought to be made at the acceptance or planning stage of an audit when circumstances at that time indicate the necessity for an EQCR. It may be that such are not apparent during the

initial stages of an audit but become so later on; where this is the case, a reviewer needs to be appointed as soon as the need for one becomes apparent. This may prove more difficult for small firms which are using an external reviewer and may be engaging the reviewer directly. However, the fact that the reviewer is external to the firm may itself be an indicator of independence and while the firm will have selected the reviewing organisation, it is unlikely to have chosen the individual that does the work.

The reviewer considers his/her independence, experience, and level of authority to deal with the issues arising, where possible at an early stage in the planning. He or she also considers the significant risks as identified in the audit planning documentation.

Before the audit report is issued, the reviewer will need to be satisfied with the quality of the audit work and the key judgements and decisions made. The reviewer will also need to confirm that he/she is not aware of any unresolved matters that would cast doubt on the significant judgements that have been made.

The review process needs to be documented (see paragraph 42 of ISQC (UK and Ireland) 1), and does not reduce the responsibilities of the engagement partner in any way.

The audit report cannot be issued where there remain unresolved differences of opinion between the engagement partner and the reviewer. At that point the firm's dispute resolution procedures should come into play.

It should be noted that audit firms are allowed to contract out the review and consultation processes to suitable individuals or organisations where necessary, following the usual safeguards eg, confidentiality undertakings, client permission, and this is expected to be helpful to smaller firms.

ENGAGEMENT DOCUMENTATION

Paragraphs 45 to 47 of ISQC (UK and Ireland) 1 outline the standard's requirements on engagement documentation with 'engagement documentation' defined in paragraph 12(b). Firms are required to complete the assembly of the audit file on a 'timely' basis which would not normally be later than 60 days after the audit report.¹⁰ Firms should have documented policies and procedures for the completion and assembly of audit files.

ISQC (UK and Ireland) 1 requires firms to retain the audit documentation for such time as required by law or regulation. ICAEW's Audit Regulations require the engagement documentation to be kept for a period of six years commencing with the date of the end of the accounting period to which the documentation relates. (NB: ISQC (UK and Ireland) 1 states that the retention period would ordinarily be no shorter than five years from the date of the audit report, so unless the client is well behind in its accounts filing, the critical point will be the six-year period required by the Audit Regulations, as above.)

The requirements mean that, within this period, auditors are prohibited from deleting or discarding documentation after the file has been assembled.

Firms need to have policies regarding the type of material which can be discarded before the end of the 60-day period for file assembly eg, superseded accounts drafts, review points cleared.

For any departures from the requirements of ISAs (UK and Ireland), the audit documentation should indicate how and why the auditors have departed from the requirements and the alternative procedures performed to meet the objective of the audit.

This is not a practical guide to the engagement level practices covered in ISA (UK and Ireland) 230 *Audit documentation*. However, in summary (see paragraph 8 of ISA (UK and Ireland) 230), audit documentation should enable an experienced auditor with no previous connection with the audit to understand:

- the work performed;
- the results and evidence obtained; and

¹⁰ It is of course good practice for the audit file to be complete for the audit engagement partner to review before signing the audit report.

- the significant matters identified and the conclusions reached thereon, and significant professional judgements made in reaching those conclusions.

The effect of this will be to enable such an experienced auditor to conduct the quality control reviews required under the monitoring provisions of ISQC (UK and Ireland) 1 and other legal and regulatory requirements.

Apart from records of audit tests performed, care should be given to documenting judgemental issues. Where significant or contentious issues are discussed with clients, it is helpful to have a policy to ensure that copies of the relevant notes are forwarded to clients in order to establish accuracy and agreement.

Oral explanations by the auditor on their own do not constitute adequate audit evidence, but they may be used to explain or clarify information in the audit documentation.

In determining the audit documentation that might be appropriate in the particular circumstances of smaller entity audits, firms should refer to the APB's Practice Note 26 *Guidance on smaller entity audit documentation* (revised version issued in December 2009).

Firms also need to have policies and procedures to ensure that the information on permanent client files is complete, in particular that the key laws and regulations of relevance to the client are properly recorded.

As part of their disaster recovery procedures, firms would be well advised to have security measures and insurance in place to deal with catastrophic events, for example a fire that destroys a firm's office. If the audit files are destroyed, ISA (UK and Ireland) 230 requires sufficient documentation of the audit work before the audit report can be given and so files would have to be assembled to do this with work being redone as required. If information from the previous year's audit has been lost, the firm will need to give particular attention to opening balances and comparatives and the requirements of ISAs (UK and Ireland) 510 and 710.

ILLUSTRATIVE POLICY AND PROCEDURE ON CONSULTATION

Consultation on audit engagements

Policy: All members of audit engagement teams are encouraged to consult within the firm, formally or informally as appropriate, on any matter where they feel the need for support.

Where a member of an audit engagement team has consulted informally and the consultant believes the matter should be the subject of a formal consultation, the firm's policies and procedures regarding formal consultation are followed.

All members of audit engagement teams are required to consult formally, in accordance with the firm's procedures set out [below], on difficult or contentious matters, for example relating to:

- an important professional judgement;
- a technical matter which is outside of their experience;
- specific identified risks;
- the need for specialist knowledge.

Formal consultation may take place within audit engagement teams or between members of audit engagement teams and other appropriate partners or specialists within the firm.

All formal consultations are documented according to the firm's procedures set out [below].

The conclusions arising from all formal consultations are documented according to the firm's procedures set out [below], and are implemented unless they give rise to a difference of opinion between the consultant(s) and the engagement partner, in which case the firm's procedures regarding differences of opinion are followed.

Procedures:

Consultation is carried out in a timely manner.

Having made a decision to consult, audit engagement team members:

- identify the person with whom they will be consulting;
- gather relevant information;
- quantify the issue if possible;
- propose a solution as far as they are able to (to act as a starting point for the consultation); and
- document the subject and outcome of the consultation including:
 - the issue;
 - the parties involved in the consultation;
 - the opinions expressed;
 - the conclusion reached;
 - the reasoning behind the conclusion (including any supporting information); and
 - how the conclusion was implemented.

The documentation of formal consultations forms part of the audit documentation and is placed on the [file/electronic equivalent].

FOR A SOLE PRACTITIONER

Consultation on audit engagements

Policy: [Name of sole practitioner] and any staff are required to consult as appropriate on matters arising from the performance of the audit engagement.

Procedure: The first point of consultation will be a senior person within the firm with relevant knowledge/expertise, where available. Where not available, [name of sole practitioner] considers consulting with an external organisation providing relevant services or consulting with ICAEW's Technical Enquiries Service. All consultation relevant to the final audit opinion is documented and kept on file.

ILLUSTRATIVE POLICY AND PROCEDURE ON THE REVIEW ASPECT OF ENGAGEMENT PERFORMANCE

Engagement quality control review (EQCR)

Policy: The firm sets criteria¹¹ for the conduct of EQCRs, those criteria being based on audit risk, public interest and specialised or regulatory nature of the audit work performed, and size of fee.

Procedure: Before the commencement of an audit, the audit engagement partner assesses the audit against the criteria set by the firm and, where indicated, reports the need for an EQCR reviewer. Such need is then considered by [named person] [the firm's senior audit partner¹²], who makes the appointment.

FOR A SOLE PRACTITIONER

Engagement quality control review (EQCR)

Policy: The firm sets criteria¹³ for the conduct of EQCRs, those criteria being based on audit risk, public interest and specialised or regulatory nature of the audit work performed, and size of fee.

Procedure: Before an audit is commenced, an assessment is made against the EQCR criteria and the results of this assessment recorded. Should an engagement meet those criteria, an EQCR reviewer with sufficient expertise and experience (who might need to be external) will be appointed [if applicable, name the external source that the firm has arranged to be available to provide the likely reviewer¹⁴].

ILLUSTRATIVE POLICY AND PROCEDURE ON THE AUDIT ENGAGEMENT DOCUMENTATION (FOR ALL FIRMS INCLUDING SOLE PRACTITIONERS)

Documentation – timely final assembly and retention of audit engagement files

Policy: Completion and retention of audit engagement documentation should comply with the requirements of paragraphs 45 and 47 of ISQC (UK and Ireland) 1.

Procedure¹⁵: All audit files are compiled in compliance with our audit system. They are assembled as near to the date of the audit report as practicable or as required, but in any event within 60 days of that date. The date of final assembly will be shown clearly on the file once assembly has been completed. They are retained for the later of six years from the balance sheet date and five years from the date of the audit report.

¹¹ The firm will of course need to set these criteria which are not shown here eg, 'we set the following criteria for the conduct of EQCR reviews: X, Y, Z, etc.'

¹² This is only likely to be relevant to, and practicable for, smaller firms. For larger firms this might, for example, be the regional managing partner or national quality control or technical partner. As stated in the above text, the reviewer should be appointed by the person or persons assigned operational responsibility for quality control or their delegate.

¹³ The firm will of course need to set these criteria which are not shown here eg, 'we set the following criteria for the conduct of EQCR reviews: X, Y, Z, etc.'

¹⁴ It would be sensible for the firm to have such an arrangement in place in advance of the need to appoint the reviewer. However, the firm should always be satisfied on a case by case basis that the proposed reviewer is suitable for carrying out the specific review ie, has the necessary expertise and experience.

¹⁵ NB: this might be one of a number of procedures under the policy.

7. MONITORING

Monitor and seek continuous improvement of the firm's system of quality control

and carry out a periodic objective inspection of a selection of completed audit engagements (paragraphs 16(f), 48–56).

The monitoring section of ISQC (UK and Ireland) 1 covers a firm's internal audit compliance reviews as also required (annually) under the ICAEW Audit Regulations. The firm's policies and procedures should include an ongoing consideration and evaluation of the firm's system of quality control, including a periodic review of a selection of completed engagements, ie 'cold file' reviews (paragraph 48).

Paragraph 48(c) of the clarified ISQC (UK and Ireland) 1 requires that those performing the engagement or the EQCR are not involved in reviewing the engagements as part of the periodic review. Determining who to use for the 'cold file' reviews might be a practical challenge for very small firms, and particularly sole practitioners and firms with only one responsible individual, where there is likely to be no independent person within the firm suitably qualified to fulfil this role. The Audit Regulations highlight the benefit that firms can gain from reviews carried out by external persons. This could be of particular value to firms at a time of rapid change in the standards and legal and regulatory framework underpinning audits.

Paragraph A66 of ISQC (UK and Ireland) 1 gives an example of three years for the review cycle. However, it also points out that the manner in which the review cycle is organised depends on a number of factors including the size of the firm. One possibility for sole practitioners and firms with only one responsible individual is to have an external review of engagements every three years (in compliance with ISQC (UK and Ireland) 1) with in-house reviews in between these to comply with the requirement of the Audit Regulations for annual reviews. But as this is a period of change with the implementation of the clarified ISAs (UK and Ireland) and ISQC (UK and Ireland) 1, it might be beneficial for firms to have the external review sooner rather than later. This would provide firms with the opportunity to examine their practices and find efficiencies and appropriate ways to manage the risks they face. Doing the review as soon as they can should mean that firms will benefit from the 'fresh pair of expert eyes' that such an external review is likely to bring during this time of change.

ISQC (UK and Ireland) 1 requires firms to communicate, at least annually, the results of the monitoring of its quality control system to engagement partners and other appropriate individuals within the firm, including the chief executive or managing board (paragraph 53). Clearly firms need to consider the urgency of any matters found in the review and the need to make appropriate changes and to communicate these as soon as possible. This requirement to communicate results may well be an item for review by an external monitoring team. It is important for firms to select an appropriate way of achieving compliance and to ensure the monitoring is carried out properly.

ICAEW Helpsheets may be of help in conducting whole firm audit compliance reviews and cold file audit compliance reviews (Helpsheets PAS4/HS05 and PAS4/HS06). ICAEW also operates an audit compliance review service for smaller firms which can consist of a review of firms' audit procedures including cold-file reviews. More information about the consultancy services is provided through the member support website address given in Appendix 4.

COMPLAINTS AND ALLEGATIONS

In the monitoring section of ISQC (UK and Ireland) 1, there are requirements regarding complaints and allegations. The firm should establish policies and procedures designed to provide it with reasonable assurance that it deals appropriately with:

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

ILLUSTRATIVE POLICY AND PROCEDURE ON THE ANNUAL COMPLIANCE REVIEW

Annual compliance review

Policy: The firm's monitoring process covers both the appropriateness of the design and the effectiveness of the operation of the system of quality control and includes:

- ongoing consideration and evaluation of the firm's system of quality control; and
- annual inspection of a selection of completed engagements.

Procedures: (ongoing consideration and evaluation of the firm's system of quality control) (extract):

An analysis is performed of:

- new developments in professional standards and regulatory and legal requirements, and how they are reflected in our policies and procedures where appropriate;
- written confirmations of compliance with policies and procedures on independence;
- CPD and training records; and
- acceptance and continuance decisions.

The reviewer, in consultation with the audit compliance partner [insert name] if necessary, determines any corrective actions to be taken and improvements to be made in the system, including improvements to our policies and procedures relating to education and training.

Appropriate firm personnel are informed of any weaknesses identified in the structure of the system itself, in the level of understanding of the system among the partners and staff, or in compliance with the system.

Procedures (engagement reviews) (extract):

Reviews of selected engagements for selected individual responsible individuals are performed on a cyclical basis, at least once every three years, for each responsible individual.

Engagements are selected at random for inspection, however the reviewer concentrates on engagements with certain specified factors¹⁶ (as set out in [place where specified]) in the first instance.

If the results of the monitoring procedures indicate that:

- a report that has been issued by the firm may have been inappropriate; or
- procedures were omitted during the performance of the engagement;

the audit compliance partner [name inserted] is informed immediately and actions are taken as appropriate.

Important matters arising are communicated to all audit partners and staff on a timely basis.

¹⁶ Factors will include size of audit and whether there is a modified audit report.

FOR A SOLE PRACTITIONER¹⁷

Quality control review

Policy: [Name of sole practitioner] is committed to providing and maintaining a high standard of audit work. One part of achieving this is carrying out regular reviews of the system of quality control including annual external inspection of a selection of completed engagements.

Procedures: [Name of sole practitioner] reviews the firm's compliance with the Audit Regulations on an annual basis.

Annual cold file reviews will be conducted by [name of external organisation] in accordance with the engagement letter agreed on [insert date].

[Name of sole practitioner] takes appropriate action based on the results of the reviews and important matters arising are communicated to all people deployed on audits on a timely basis.

ILLUSTRATIVE POLICY AND PROCEDURE ON THE COMPLAINTS ASPECT OF MONITORING

Complaints

Policy: The firm is committed to providing a high-quality service to clients, and takes all complaints and allegations against the firm very seriously. The firm will deal on a timely basis with all complaints and allegations that the work performed by the firm fails to comply with professional standards and regulatory and legal requirements.

Procedure: All complaints of whatever nature are reported to [insert name of complaints partner] using the firm's standard form, who forwards written details of valid complaints as soon as possible to [insert name of the managing partner], and to [insert name of the professional indemnity partner], for their respective action. Periodic reports of complaints are circulated to all partners and trends identified for further advice, training, disciplinary action or internal quality control systems changes.

FOR A SOLE PRACTITIONER

Complaints

Policy: [Name of sole practitioner] is committed to providing a high-quality service to clients, and takes all complaints and allegations against the firm very seriously. [Name of sole practitioner] will deal on a timely basis with all complaints and allegations that the work performed by the firm fails to comply with professional standards and regulatory and legal requirements.

Procedure: All complaints of whatever nature are reported to [name of sole practitioner] who takes action as appropriate. This might include the need for further advice, training, disciplinary action or internal quality control systems changes.

¹⁷ NB: as with all the examples in this guide, this example is purely illustrative for a sole practitioner who has chosen to undertake external annual reviews. The ISQC (UK and Ireland) 1 requirements regarding these reviews are covered earlier in this section.

APPENDIX 1: SOME KEY POINTS ABOUT ISQC (UK AND IRELAND) 1

The standard's objective (paragraph 11) is as follows:

'The objective of the firm is to establish and maintain a system of quality control to provide it with reasonable assurance that:

- (a) The firm and its personnel comply with professional standards and applicable legal and regulatory requirements; and
- (b) Reports issued by the firm or engagement partners are appropriate in the circumstances.'

In the context of ISQC (UK and Ireland) 1, 'reasonable assurance' means a high, but not absolute, level of assurance (paragraph 12(p)).

Paragraph 13 of the standard requires those within the firm responsible for establishing and maintaining the firm's system of quality control to have an understanding of the entire text of ISQC (UK and Ireland) 1 and to apply its requirements properly.

A system of quality control consists of policies and procedures. Its nature will depend on factors such as the size and operating characteristics of the firm, and whether it is part of a network (paragraph 4). In all cases, the policies and procedures adopted need to be tailored as appropriate, while still retaining the principles of ISQC (UK and Ireland) 1. Paragraphs 14 and A1 make it clear that firms do not have to comply with those requirements that are not relevant, for example sole practitioners with no staff do not need policies for the assignment of staff to audit (paragraph 31).

Paragraph 15 requires firms to consider whether there are particular matters or circumstances that mean the firm should establish additional policies and procedures to meet the stated objective as above.

ISQC (UK and Ireland) 1 is designed to enhance quality, and firms will only achieve and maintain profitability in the long term if they provide a quality service.

Key features of ISQC (UK and Ireland) 1 include:

- the requirement to document is in places specific, prescriptive and detailed;
- the firm's chief executive or senior partner or managing board (or equivalent) is to assume ultimate responsibility for the firm's system of quality control;
- emphasis on the content and detail of the firm's formal policies and procedures; and
- a list of what needs to be considered during an engagement quality control review (EQCR) and requirements regarding its nature, timing, and documentation.

Overall, when applying ISQC (UK and Ireland) 1 to their own circumstances, firms need to consider:

- the level of detail needed;
- the nature of the communications to principals and staff required; and
- the appropriate level of documentation necessary.

There is clearly an important connection between ISQC (UK and Ireland) 1 and ISA (UK and Ireland) 220 *Quality control for an audit of financial statements* (ISA (UK and Ireland) 220). However, the latter applies in respect of individual audits, where the responsibility rests with the engagement partner rather than the firm. The engagement partner has a number of specific responsibilities outlined in ISA (UK and Ireland) 220 which relate to the overall quality of work for each audit engagement.

APPENDIX 2: SOME FREQUENTLY ASKED QUESTIONS

As a sole practitioner do I really need to document my system of quality control?

Yes you do. This need not be onerous though. In many cases it will involve describing what you already do rather than inventing new policies and procedures.

We have standard documentation covering quality control within the firm's audit compliance manual which was written by an external provider. Is there anything more we need to do?

The standard documentation can be used as a base but it is important for the firm itself to do an ISQC (UK and Ireland) 1 exercise to ensure that it has covered all the specific requirements of the standard. The firm should consider how to add to the manual and adapt it to reflect the particular circumstances of the firm. Relevant points of contact within the firm and any sources of external advice should be included. As stated in the section on key area 1, the ISQC (UK and Ireland) 1 exercise for a smaller firm might be relatively straightforward, comprising of bringing together (or referring to) the various material that is available elsewhere within the firm. You should also consider the issue of maintenance. It will be important to ensure both that the documentation is kept up to date and that all relevant personnel are advised of any updates. For example, you might ensure that all staff sign for new updates or run training sessions every time the documentation is updated.

We are a small firm with three audit partners. Should one of us be appointed as a specific quality control partner?

Yes, it may be a good idea for one partner to be assigned the operational responsibility for the system of quality control. However, ultimate responsibility for the system of quality control always lies with a firm's managing partner (or equivalent).

What are the particular challenges for firms with more than one office? Do we need a fully integrated system that is centrally controlled and monitored?

It is important that the firm's procedures are standardised and applied on a consistent basis in each of the offices of the firm. This makes it easier to exercise the ultimate responsibility for the system of quality control of the firm as a whole which, as stated above, rests with the managing partner or equivalent. It also makes it easier for staff transferring between offices.

We realise that we should do more to document what we do on acceptance and continuance. What should we do beyond completing the standard forms we currently have for this?

The firm might consider developing an aide-mémoire covering the various issues to consider on acceptance and continuance and what should be documented. It is important to properly incorporate the need for other considerations (as highlighted in the section on key area 4) to be documented eg, on industry knowledge and specialist needs, whether it is an unusual engagement in terms of size or nature, and whether there are ethical threats.

Our firm only has a small number of audits now, although we remain committed to continuing to provide this service to our clients. However, we are finding it increasingly difficult ensuring that all partners and staff are fully trained and prepared to carry out this audit work. Any suggestions?

It might be beneficial, for quality and efficiency, for firms in this position to use only audit 'specialists' for this work so that they are properly trained and developed as needed for the firm's audit work.

I am a sole practitioner based in an area where there isn't any obvious source of audit related expertise eg, to help with consultation issues or reviews. I'm not aware of any other local firm that is still providing audit services.

In situations where consultation or review services are needed, the practitioner might consider engaging appropriate qualified external assistance. If the practitioner is uncertain regarding a technical accounting or auditing matter he or she could refer to the various member support services available from ICAEW: www.icaew.com/membersupport (see Appendix 4).

We are a small firm and realise that we need to substantially rewrite our audit procedures, particularly for the two specialist audits that we do. What is the best course of action for us?

First of all the firm should consider whether it is in a position to continue as auditor, particularly for the specialist audits. This will include assessment of whether the firm has staff with the necessary knowledge and experience. In terms of developing the systems and procedures that will be needed to carry out these audits, the firm might consider purchasing a proprietary system and using this as appropriate. It could well be that the internal cost of developing and maintaining the firm's own systems will be greater and calling on external help might also reduce the risks faced by the firm embarking on these audits.

We are a small firm. Do we have to perform Engagement Quality Control Reviews (EQCRs)?

Possibly. What you do have to do is establish a policy for the type of engagement that would require such a review, based on considerations of risk, size, complexity and potential public interest. It is worth emphasising that all audits of 'listed' entities must have an EQCR and this includes all AIM and PLUS clients whatever their size. Should you accept a new engagement that meets the criteria you have determined (or should an existing engagement develop one or more of those criteria), then you will need to consider engaging an external EQCR reviewer with the appropriate expertise and experience. The requirements relating to the criteria for the eligibility of EQCR reviewers are given in paragraphs 39 to 41 of ISQC (UK and Ireland) 1 and the guide covers this topic in the section on key area 6. The objectivity of the EQCR reviewer is of paramount importance. You may be able to come to an arrangement with another firm of auditors or with an external organisation offering reviewing services if they are suitably qualified for your purpose.

I am a sole practitioner and have identified the need for an EQCR reviewer on one of my audits. I'm planning to use a suitable external reviewer this year for the first time. Is there anything I should be doing to ensure this works effectively?

You will need to consider how the process should be managed and this will include the need for appropriate communication at the relevant stages of the process, including at the planning stage.

We think that we might need to appoint an EQCR reviewer for one of our audits. Assuming we do appoint someone for this purpose, can this EQCR reviewer also carry out the cold file reviews for audits of this client?

As explained in section 7, those performing the engagement or the EQCR should not be involved in reviewing the engagements as part of the ISQC (UK and Ireland) 1 periodic review. This highlights the self-review threat that would exist for the EQCR reviewer, just as much as for the engagement partner, if either were to carry out the cold file reviews.

Our firm is keen to maximise the benefit we gain from the annual (cold file) reviews after they've been done. Any suggestions on what we might do?

It is important to properly record the findings from the review of completed engagements and to ensure that appropriate actions are taken based on the findings. It is helpful to have a procedure defining the responsibility for the management, documentation and conclusions on the annual (cold file) reviews including how identified weaknesses and training needs will be acted upon, including in the planning for next year's audits and training activity. It should be explained how the results will be communicated to partners and staff and how matters will be monitored so that necessary training does happen and improvements are made.

I am a sole practitioner and will be using an external company for my monitoring (cold file) reviews. What evidence will I need regarding these reviews?

You would be well advised to ensure that you will be provided with a report in a form you regard as appropriate as part of the terms of the engagement. Also you will need to demonstrate how you are dealing with any issues identified requiring action.

We are a small firm and we have a number of 'assurance' type engagements such as independent examination for charities. Are the standard and the guide relevant to these?

As explained in the Foreword, ISQC (UK and Ireland) 1 applies to audit and also to reporting in connection with investment circulars and providing other assurance services where they relate to activities that are reported in the public domain and are therefore in the public interest.

There is no requirement for ISQC (UK and Ireland) 1 compliance for other engagements in the UK outside of this scope but don't forget that ICAEW's Practice Assurance Standard 4 is about quality control and will apply. The IAASB version of the standard does apply to 'reviews of financial statements, and other assurance and related services engagements'. It is hoped that much of the guidance in this publication is still helpful for firms carrying out all of these types of engagement, including those beyond the scope of ISQC (UK and Ireland) 1.

APPENDIX 3: MEMBERS OF THE WORKING GROUP

Chair: Gill Spaul, Moore Stephens Europe

Andrew Güntert, Mercia

Nicole Kissun, PKF

Alex Peal, James Cowper

Stephen Thomas

Peter Upton, sole practitioner

Secretary: Chris Cantwell, ICAEW Audit and Assurance Faculty

The working group also benefited from the participation of other ICAEW staff from the Professional Standards Department, Quality Assurance Department and the Audit and Assurance Faculty.

APPENDIX 4: SOURCES OF INFORMATION FOR FIRMS

Publications, other services and website addresses:

ICAEW AUDIT AND ASSURANCE FACULTY

Audit & Beyond monthly newsletter.

Various publications of interest to external auditors, including on the implementation of the clarified ISAs.

www.icaew.com/aaf

www.isaaudit2010.com

ICAEW MEMBER SERVICES

Practice Helpsheets (including for whole firm audit compliance reviews and cold file audit compliance reviews).

Audit compliance review service. This is for smaller audit firms and can consist of a review of a firm's audit procedures including cold-file reviews. The service offers feedback and guidance for improving efficiency, quality and profitability. There is more information at the website address below (go to 'practice support' and 'consultancy services') or call +44 (0)1908 248025 (option 3) or email practice.services@icaew.com.

www.icaew.com/membersupport

ICAEW PROFESSIONAL STANDARDS DEPARTMENT

Audit Regulations and Guidance¹⁸

Audit News

www.icaew.com/auditnews

ICAEW ETHICS SUPPORT

ICAEW Code of Ethics, guidance, publications and support for resolving ethical problems

Helpsheets, frequently asked questions, ethics helpline

www.icaew.com/ethics

www.icaew.com/ethicsadvice

AUDITING PRACTICES BOARD (APB)

Standards and Guidance for Auditors (includes the text of ISQC (UK and Ireland) 1, Statement of Scope and Authority of APB Pronouncements, all ISAs (UK and Ireland), Practice Note 26 and APB Ethical Standards, including Provisions Available for Small Entities. Individual Standards and other pronouncements are also available to download free from the APB's website.

www.frc.org.uk/apb

INTERNATIONAL FEDERATION OF ACCOUNTANTS (IFAC) AND THE INTERNATIONAL AUDIT AND ASSURANCE STANDARDS BOARD (IAASB)

The IAASB has provided a **clarity centre** with various support materials on the clarified standards including **ISA modules**.

The IFAC Small and Medium Practices Committee has produced a lengthy *Guide to Quality Control for Small- and Medium-Sized Practices* which includes sample quality control manuals.

<http://web.ifac.org/clarity-center/index>

<http://web.ifac.org/publications/small-and-medium-practices-committee>

¹⁸ The latest version of the Audit Regulations and Guidance (incorporating all changes since first issued) is available from the above *Audit News* link. The Audit Regulations apply to all firms registered with the ICAEW as eligible for appointment as company auditor under the Companies Act. Chapter 3 covers how a firm operates its overall audit practice.

As a world-class professional accountancy body, ICAEW provides leadership and practical support to over 134,000 members in more than 160 countries, working with governments, regulators and industry to maintain the highest standards.

Our members provide financial knowledge and guidance based on the highest technical and technical standards. They are trained to challenge people and organisations to think and act differently, to provide clarity and rigour, and so help create and sustain prosperity. ICAEW ensures these skills are constantly developed, recognised and valued.

Because of us, people can do business with confidence.

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