

# Auditing Standards Update: So Much for the Idea of a Super SAS

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# AICPA Auditing Standards (GAAS)

- ▶ 1<sup>st</sup> set of auditing standards that typically apply to state and local governmental audits
- ▶ Not much is happening here
- ▶ Last most *significant* auditing standard issued by the AICPA was SAS 145, *Understanding the Entity and Its Environment and Assessing the Risks of Material Misstatement* (talked about at length last year)

# AICPA ASB – Recent Auditing Standards and effective dates

SAS No.	Topic	AU– C Section Affected	Effective Date
<u>142</u>	Audit Evidence	500 and various other AU–Cs	Audits of periods ending on or after 12/15/2022
<u>143</u>	Auditing Accounting Estimates and Related Disclosures	540 and various other AU–Cs	Audits of periods ending on or after 12/15/2023
<u>144</u>	Use of Specialists and Use of Pricing Information	501, 540, and 620	Audits of periods ending on or after 12/15/2023
<u>145</u>	Risk Assessment	315 and various other AU–Cs	Audits of periods ending on or after 12/15/2023

# AICPA ASB – Recent Auditing Standards

SAS No.	Topic	AU– C Section Affected	Effective Date
<u>146</u>	Quality Management for an Engagement Conducted in Accordance With Generally Accepted Auditing Standards	220 and various other AU–Cs	Audits of periods beginning on or after 6/30/2025
<u>147</u>	Inquiries of the Predecessor Auditor Regarding Fraud and Noncompliance With Laws and Regulations	210	Audits of periods beginning on or after 6/30/2023
<u>148</u>	Amendments to AU–C Section 935	935	Various (to align with effective dates of SAS 142 and 145)
<u>149</u>	Special Considerations – Audits of Group Financial Statements (Including the Work of Component Auditors and Audits of Referred-to Audits)	600 and various other AU–Cs	Audits of periods ending on or after 12/15/2026

# Auditor Risk Assessments

- ▶ While risk assessment may seem boring, an inappropriate risk assessment will most likely lead to a substandard audit
- ▶ A substandard audit will most likely lead to trouble
- ▶ We hate trouble
- ▶ The risk assessment standards have been given a renewed focus through the AICPA's Enhanced Audit Quality Initiative, as well as through Peer Review

# Basic concept of auditor risk assessments

- ▶ You can't properly apply the risk assessment standards if you don't understand the audit risk model
- ▶ While many think they understand the model, the results of Peer Review, IG desk reviews, and other audit quality sampling projects say otherwise
- ▶ Now is the time to reinforce your understanding of each element of the model, and how the model is used in determining the nature, timing and extent of both the risk assessment auditing procedures and the further auditing procedures

# Problems with risk assessment

- ▶ Many firms still simply select auditing procedures from standardized audit programs with little or no thought of whether the procedures selected are responsive to the risks of material misstatement
- ▶ Other firms will have a basic or core set of procedures that they perform for each area, and additional procedures to choose from for additional assurance if needed, and then finally more procedures to choose from if there are additional risks



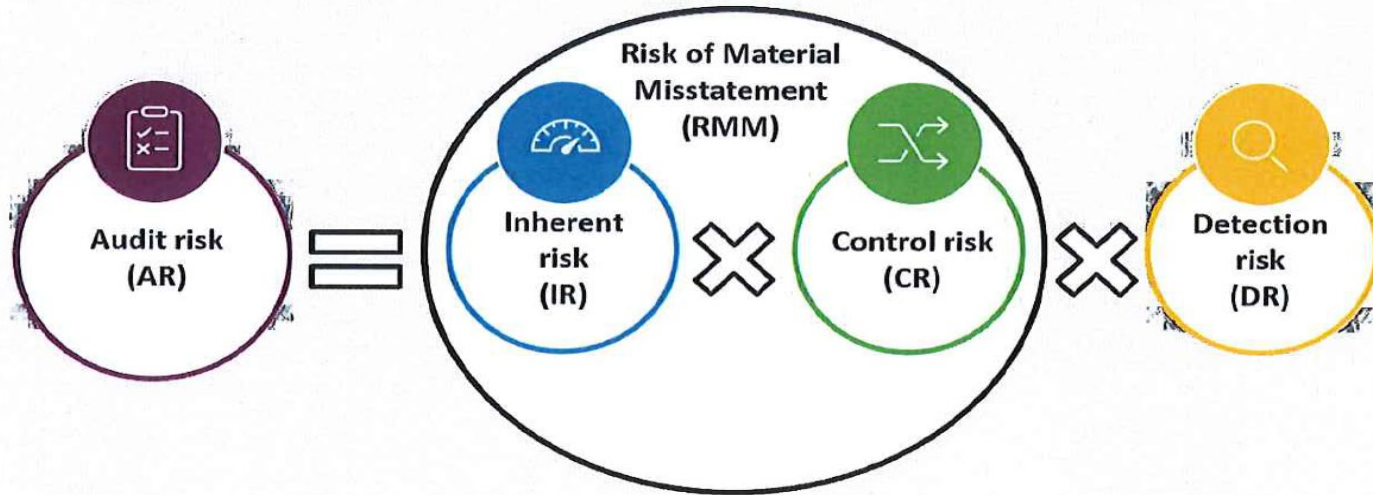
# Problems with risk assessment

- ▶ While the previous slide's second bullet methodology isn't necessarily a bad thing, those illustrative audit procedures are no substitute for truly understanding the risks of material misstatement and using professional judgment to select and tailor procedures that are responsive to the risks AND which reduce audit risk to an acceptably low level



# Audit Risk Model

The audit risk model is expressed as follows:



**Audit risk** is the risk that the firm will issue an unmodified report when, in fact, there is a material misstatement in the financial statements.

**Inherent risk** is the risk of material misstatement in an assertion, an account balance, or disclosure before consideration of any related controls.

**Control risk** is the risk that the entity's controls will not prevent or detect and correct a material misstatement.

**Detection risk** is the risk that the procedures performed by the auditor will not detect a misstatement that exists and that could be material.

As a reminder, auditors only affect detection risk since control and inherent risks are entity risks that exist independent of the audit and the auditor.

$$AR = (IR \times CR) \times DR$$

$$3\% = (? \times ?) \times ?$$

There are multiple ways to get there; here a just a few:

$$3\% = (50\% \times 100\%) \times 6\%, \text{ or}$$

$$3\% = (100\% \times 100\%) \times 3\%, \text{ or}$$

$$3\% = (10\% \times 60\%) \times 50\%$$

$$3\% = (60\% \times 10\%) \times 50\%$$

Target is 3% AR. Most can live with that

Is the testing of internal controls *required* by any of the above formulas?

# Another way to look at it

$$AR = (IR \times CR) \times DR$$

Can the following equation work?

$$L = (L \times H) \times H$$

Yes, but how does it work?

It works because the font sizes are different!

$$L = (\text{L} \times H) \times H$$

$$L = \text{L} \times H$$

# New SAS 145 on Risk Assessment

- ▶ Technically titled “Understanding the Entity and Its Environment and Assessing the Risks of Material Misstatement”

# New SAS 145 on Risk Assessment

- ▶ This SAS's goal was to enhance the auditing standards relating to the auditor's risk assessment and intends to enable auditors to appropriately address the following:
  - a. Understanding the entity's system of internal control, in particular, relating to the auditor's work effort to obtain the necessary understanding
  - b. Modernizing the standard in relation to IT considerations, including addressing risks arising from entity's use of IT
  - c. Determining risks of material misstatements, including *significant risks* (new definition)
- ▶ SAS will be effective for audits of financial statements for periods ending on or after December 15, 2023.

# Big changes or little changes?

- ▶ The ASB did not seek to fundamentally change the key concepts underpinning audit risk as the ASB continues to have the view that the audit risk model is fundamentally sound.
- ▶ Rather, the ASB focused on how certain aspects of the identification and assessment of the risks of material misstatement can be clarified and improved in order to drive better risk assessments and, therefore, enhance audit quality.

# Public Interest Issues Addressed in the Proposed SAS

- ▶ Scalability
- ▶ Modernizing and Updating AU–C Section 315 for an Evolving Business Environment
- ▶ Automated Tools and Techniques
- ▶ Information Technology
- ▶ Fostering Independence of Mind and Professional Skepticism
- ▶ The Auditor’s Considerations Relating to Fraud



# Understanding the Entity and Its Environment

- ▶ Focusing on the Applicable Financial Reporting Framework in Identifying Risks of Material Misstatement

# Understanding the Entity's System of Internal Control

- ▶ Terms Used to Describe Aspects of the Entity's System of Internal Control
- ▶ Understanding Internal Control Through Understanding the Five Components of Internal Control
- ▶ Work Effort for Understanding Each of the Components of Internal Control
- ▶ Controls That Address the Risks of Material Misstatement
- ▶ Enhanced Guidance Related to IT
- ▶ Other Matters Relevant to Understanding the Entity's System of Internal Control

# Identifying and Assessing the Risks of Material Misstatement

- ▶ Identifying and Assessing the Risks of Material Misstatement
  - Spectrum of Inherent Risk (fancy name for our font size example); the word “spectrum” is used 38 times in this SAS, so they must think it’s a big deal
- ▶ Relationship of Concepts With AU–C Section 540
- ▶ Significant Risks
- ▶ Identified and Assessed Risks of Material Misstatement at the Financial Statement Level
- ▶ Stand–Back and Paragraph .18 of AU–C section 330

# Stand Back requirement

- ▶ A new "stand-back" requirement intended to drive an evaluation of the completeness of the auditor's identification of significant classes of transactions, account balances, and disclosures (see paragraph 5.41)

# What's a significant class of transactions, account balance or disclosure?

- ▶ A class of transactions, account balance, or disclosure for which there is one or more *relevant* assertions.
  - What does relevant mean?
    - An assertion about a class of transactions, account balance, or disclosure is relevant when it has an identified risk of *material* misstatement.
    - A risk of material misstatement exists when (a) there is a reasonable possibility of a misstatement occurring (that is, its likelihood), and (b) if it were to occur, there is a reasonable possibility of the misstatement being material (that is, its magnitude).

# Conforming amendment

- ▶ A conforming amendment to perform substantive procedures for each relevant assertion of each significant class of transactions, account balance, and disclosure, regardless of the assessed level of control risk (rather than for all relevant assertions related to each material class of transactions, account balance, and disclosure, irrespective of the assessed risks of material misstatement, as previously required)

# Significant risks

An identified risk of material misstatement for which the assessment of inherent risk is close to the upper end of the spectrum of inherent risk due to the degree to which inherent risk factors affect the combination of the likelihood of a misstatement occurring and the magnitude of the potential misstatement should that misstatement occur, or that is to be treated as a significant risk in accordance with the requirements of other AU-C sections



# Audit Documentation

- ▶ Documentation of key matters
- ▶ Rationale for the significant judgments made in identifying and assessing the risks of material misstatement
- ▶ *Requires* that the auditor assess inherent risk and control risk separately

# Let's talk about Quality Management Standards

# What's changing

- ▶ 4 new standards
- ▶ Moving from a policies–based approach to a risk–based approach
- ▶ Revised components of the system of quality management with two entirely new components

# Who is affected

- ▶ Every firm/organization that performs engagements in accordance with the SASs, SSARSs, SSAEs
- ▶ Deadline:
  - Implementation of these new standards is required by December 15, 2025

# 4 New Standards

- ▶ A Firm/Organization's System of Quality Management
- ▶ Engagement Quality Reviews
- ▶ Quality Management for an Engagement Conducted in Accordance with Generally Accepted Auditing Standards
- ▶ Quality Management for an Engagement Conducted in Accordance with Statements for Accounting and Review Services

# SQMS No. 1

## ▶ 8 Components

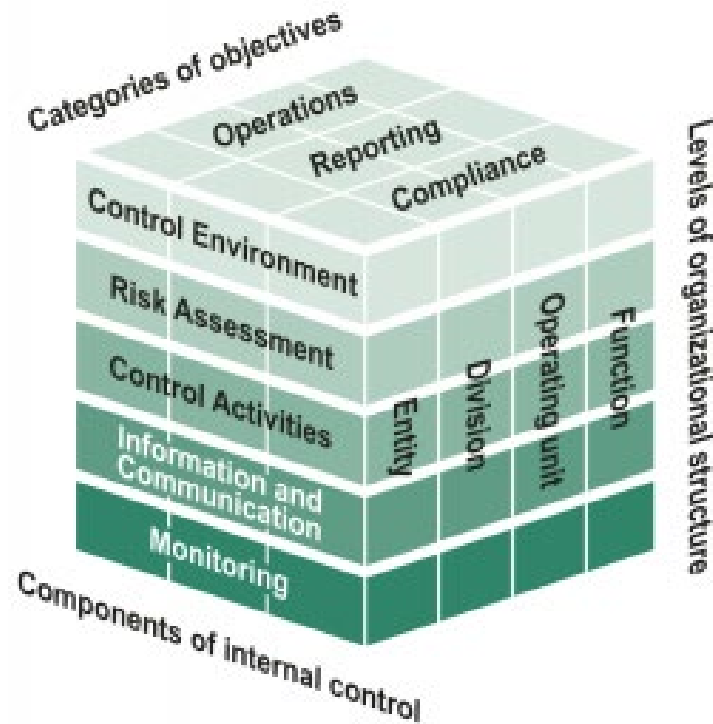
- 1. The Firm/Organization's risk assessment process (new component)
- 2. Governance and leadership (new and revised)
- 3. Relevant ethical requirements (new and revised)
- 4. Acceptance and continuance of client relationships and specific engagements (new and revised)
- 5. Engagement performance (new and revised)
- 6. Resources (new and revised)
- 7. Information and communication (new component)
- 8. Monitoring and remediation process (new and revised)

# Risk Assessment process

- ▶ Establish quality objectives
  - ▶ Identify and Assess Quality Risks
  - ▶ Design and Implement Responses
- 
- ▶ Note: Establish policies or procedures to identify information indicating the need for additional or modifications to quality objectives, quality risks or responses



# Sound Familiar?



Sources: COSO and GAO. | GAO-14-704G

# Objectives and Risk

- ▶ Remember you may have your own (Tailored)
  - Sub-objectives
  - State Laws/Regulations
  - Business model-characteristics
    - Type of work (audit, examinations, Yellowbook, Single Audit)
  - Network Firm impact – use of 3<sup>rd</sup> parties
  - Fit your practice
  - Scalable
- ▶ *Minimum inverse to identified/required objectives*
- ▶ *Consider R.A. living breathing document you must care for.*

# Governance & Leadership

QO #	Ref:	Quality Objectives
GOV QO-1	QM sec. 10, par. .29a	<p>The firm demonstrates a commitment to quality through a culture that exists throughout the firm, which recognizes and reinforces the following:</p> <ul style="list-style-type: none"> <li>• The firm's role in serving the public interest by consistently performing quality engagements</li> <li>• The importance of professional ethics, values, and attitudes</li> <li>• The responsibility of all personnel for quality relating to the performance of engagements or activities within the SOQM and their expected behavior</li> <li>• The importance of quality in the firm's strategic decisions and actions, including the firm's financial and operational priorities</li> </ul>
GOV QO-2	QM sec. 10, par. .29b	Leadership is responsible and accountable for quality.
GOV QO-3	QM sec. 10, par. .29c	Leadership demonstrates a commitment to quality through its actions and behaviors.
GOV QO-4	QM sec. 10, par. .29d	The organizational structure and assignment of roles, responsibilities, and authority is appropriate to enable the design, implementation, and operation of the firm's SOQM.
GOV QO-5	QM sec. 10, par. .29e	Resource needs, including financial resources, are planned for, and resources are obtained, allocated, or assigned in a manner that is consistent with the firm's commitment to quality.

Your firm may have additional or subobjectives to fit you environment and risk

# Governance & Leadership

## GOV QO-1

The firm demonstrates a commitment to quality through a culture that exists throughout the firm, which recognizes and reinforces the following:

- i. The firm's role in serving the public interest by consistently performing quality engagements
- ii. The importance of professional ethics, values, and attitudes
- iii. The responsibility of all personnel for quality relating to the performance of engagements or activities within the system of quality management and their expected behavior
- iv. The importance of quality in the firm's strategic decisions and actions, including the firm's financial and operational priorities

QO#	QRi #	Quality Risk	Likelihood	Impact	Quality Risk	Quality Response	QRe#
GOV QO-1	GOV QRi-3	I do not recognize or reinforce the importance of professional ethics, values, and attitudes.	Low	High	Yes	Policy: I internalize the message that quality is essential in performing engagements.	GOV QRe-3
GOV QO-1	GOV QRi-5	I do not recognize or reinforce the importance of quality in my firm's strategic decisions and actions, including my firm's financial and operational priorities.	Medium	High	Yes	I consider the costs associated with a strong SOQM, such as the costs of maintaining necessary competency, practice aids and professional subscriptions, and hiring consultants and engagement quality reviewers, as an investment. I consider these costs when determining rates and fees so that financial and operational priorities will not override the quality of work performed.	GOV QRe-5.02

# Relevant Ethical Requirements

QO#	Ref:	Quality Objectives
RER QO-1	QM sec. 10, par. .30a	<p>The firm and its personnel</p> <ul style="list-style-type: none"><li>i. understand the relevant ethical requirements to which the firm and the firm's engagements are subject.</li><li>ii. fulfill their responsibilities in relation to the relevant ethical requirements to which the firm and the firm's engagements are subject.</li></ul>
RER QO-2	QM sec. 10, par. .30b	<p>Others, including the network, network firms, individuals in the network or network firms, or service providers, who are subject to the relevant ethical requirements to which the firm and the firm's engagements are subject</p> <ul style="list-style-type: none"><li>i. understand the relevant ethical requirements that apply to them, and</li><li>ii. fulfill their responsibilities in relation to the relevant ethical requirements that apply to them.</li></ul>

# Relevant Ethical Requirements

QO#	QRi #	Quality Risk	Likelihood	Impact	Quality Risk	Quality Response	QRe#
RER QO-1	RER QRi-3	I do not receive, investigate, or resolve complaints and allegations about failures to perform work in accordance with professional standards and applicable legal and regulatory requirements or noncompliance with the firm's policies or procedures established in accordance with the firm's SOQM.	Medium	High	Yes	I consider all complaints raised, consult externally as appropriate, and document their resolution.	RER QRe-8.03
RER QO-1	RER QRi-4	Consultation and evaluation of identified independence matters results in an incorrect conclusion.	Low	High	Yes	I document the resolution of ethical matters when consultation has occurred, including consultation of professional literature or the AICPA Ethics Hotline.	RER QRe-1.03

# Acceptance & Continuance

QO #	Ref:	Quality Objectives
EAC QO-1	QM sec. 10, par. .31a(i)	Firm judgments about whether to accept or continue a client relationship or specific engagement are appropriate based on information obtained about the nature and circumstances of the engagement and the integrity and ethical values of the client (including management and, when appropriate, those charged with governance) that is sufficient to support such judgments.
EAC QO-2	QM sec. 10, par. .31a(ii)	Firm judgments about whether to accept or continue a client relationship or specific engagement are appropriate based on the firm's ability to perform the engagement in accordance with professional standards and applicable legal and regulatory requirements.
EAC QO-3	QM sec. 10, par. .31b	The financial and operational priorities of the firm do not lead to inappropriate judgments about whether to accept or continue a client relationship or specific engagement.



# Acceptance & Continuance

QO#	QRi #	Quality Risk	Likelihood	Impact	Quality Risk	Quality Response	QRe#
EAC QO-1	Firm judgments about whether to accept or continue a client relationship or specific engagement are appropriate based on information obtained about the nature and circumstances of the engagement and the integrity and ethical values of the client (including management, and, when appropriate, those charged with governance) that is sufficient to support such judgments.						
EAC QO-1	EAC QRi-2	The firm does not understand the entity's industry for which the engagement is being undertaken, as well as the relevant regulatory factors.	Low	High	Yes	The firm accepts engagements that meet the firm's criteria as high risk only when the firm has, or is willing to make, the investment to acquire the necessary competency. The firm acknowledges that accepting a high-risk engagement entails assigning more experienced staff, may necessitate the use of external resources, and requires that an EQ review be performed.	EAC QRe-2.03
EAC QO-2	EAC QR1-34	The engagement partner accepts or continues an engagement without appropriately identifying and evaluating the effect of nonattest services on firm independence.	Medium	Medium	Yes	The firm considers the risk associated with providing professional services in particular circumstances, including evaluating factors that have a bearing on management's integrity. The firm only accepts or continues engagements and client relationships when it concludes that the risk is at an acceptable level.	EAC QRe-1

# Engagement Performance

QO #	Ref:	Quality Objectives
EP QO-1	QM sec. 10, par. .32a	Engagement teams understand and fulfill their responsibilities in connection with the engagements, including, as applicable, the overall responsibility of engagement partners for managing and achieving quality on the engagement and being sufficiently and appropriately involved throughout the engagement.
EP QO-2	QM sec. 10, par. .32b	The nature, timing, and extent of direction and supervision of engagement teams and review of the work performed is appropriate based on the nature and circumstances of the engagements and the resources assigned or made available to the engagement teams, and the work performed by less experienced engagement team members is directed, supervised, and reviewed by more experienced engagement team members.
EP QO-3	QM sec. 10, par. .32c	Engagement teams exercise appropriate professional judgment and, when applicable to the type of engagement, maintain professional skepticism.
EP QO-4	QM sec. 10, par. .32d	Consultation on difficult or contentious matters is undertaken and the conclusions agreed are implemented.
EP QO-5	QM sec. 10, par. .32e	Differences of opinion within the engagement team, or between the engagement team and the EQ reviewer or individuals performing activities within the firm's SOQM, are brought to the attention of the firm and resolved.
EP QO-6	QM sec. 10, par. .32f	Engagement documentation is assembled on a timely basis after the date of the engagement report and is appropriately maintained and retained to meet the needs of the firm and comply with law, regulation, relevant ethical requirements, or professional standards.

# Engagement Performance

QRe#	Quality Response	Note, Tip, or Warning
Engagement Performance		
EP QRe-8	<p><b>Policy:</b> The firm has criteria for determining whether an EQ review should be performed, evaluates all engagements against the criteria, performs an EQ review for all engagements that meet the criteria, and completes the review before the report is released.</p>	<p><b>NOTE:</b> This is a required response. [QM sec. 10, par. .35f and QM sec. 20 par. .24b]</p> <p><b>TIP:</b> If your acceptance and continuance policies and procedures limit engagement risk, the need for an EQ review may be diminished.</p> <p><b>WARNING:</b> Criteria that are not responsive to the structure and nature of the firm's practice are not appropriate.</p>
EP QRe-8.01	<p>The firm's criteria for requiring that an EQ review be performed are based on the firm's assessment of which engagements would most benefit from an independent review, taking into account the structure and nature of the firm's practice.</p>	<p><b>WARNING:</b> When setting criteria for an EQ review, it is critical that the firm carefully consider which engagements have the highest risk of NOT being performed in accordance with the standards or that the report will NOT be appropriate in the circumstances. Consider the engagements that the firm performs in setting the criteria and not only engagements that are clearly outside the firm's expertise. Recognize that risk factors to the firm change over time and the firm's criteria for an EQ review may need to change accordingly.</p>

# Resources

QO #	Ref:	Quality Objectives
RES QO-1	QM sec. 10, par. .33a	Personnel are hired, developed, and retained and have the competence and capabilities to <ul style="list-style-type: none"> <li>i. consistently perform quality engagements, including having knowledge or experience relevant to the engagements the firm performs, or</li> <li>ii. perform activities or carry out responsibilities in relation to the operation of the firm's systems of quality management.</li> </ul>
RES QO-2	QM sec. 10, par. .33b	Personnel demonstrate a commitment to quality through their actions and behaviors, develop and maintain the appropriate competence to perform their roles, and are held accountable or recognized through timely evaluations, compensation, promotion, and other incentives.
RES QO-3	QM sec. 10, par. .33c	Individuals are obtained from external sources (that is, the network, another network firm, or a service provider) when the firm does not have sufficient or appropriate personnel to enable the operation of the firm's SOQM or performance of engagements.
RES QO-4	QM sec. 10, par. .33d	Engagement team members are assigned to each engagement, including an engagement partner, who have appropriate competence and capabilities, including being given sufficient time, to consistently perform quality engagements.
RES QO-5	QM sec. 10, par. .33e	Individuals who have appropriate competence and capabilities, including sufficient time, are assigned to perform activities within the SOQM.
RES QO-6	QM sec. 10, par. .33f	Appropriate technological resources are obtained or developed, implemented, maintained, and used to enable the operation of the firm's SOQM and the performance of engagements.
RES QO-7	QM sec. 10, par. 33g	Appropriate intellectual resources are obtained or developed, implemented, maintained, and used to enable the operation of the firm's SOQM and the consistent performance of quality engagements, and such intellectual resources are consistent with professional standards and applicable legal and regulatory requirements, where applicable.
RES QO-8	QM sec. 10, par. 33h	Human, technological, or intellectual resources from service providers are appropriate for use in the firm's SOQM and in the performance of engagements, taking into account preceding quality objectives RES QO-4 through RES QO-7.

# Resources

## RES Q0-1

Personnel are hired, developed, and retained and have the competence and capabilities to

- i. consistently perform quality engagements, including having knowledge or experience relevant to the engagements the firm performs, or
- ii. perform activities or carry out responsibilities in relation to the operation of the firm's system of quality management.

Q0#	QRI #	Quality Risk	Likelihood	Impact	Quality Risk	Quality Response	QRe#
RES Q0-1	RES QRI-2	Personnel, including partners, do not have the competence and capabilities to perform activities or carry out responsibilities in relation to the operation of the firm's SOQM.	Low	High	Yes	The firm has sufficient personnel with the competence, capabilities, and commitment to ethical principles necessary to perform engagements in accordance with professional standards and applicable legal and regulatory requirements and enable the firm to issue reports that are appropriate in the circumstances.	RES QRe-1

## RES Q0-2

Personnel demonstrate a commitment to quality through their actions and behaviors, develop and maintain the appropriate competence to perform their roles, and are held accountable or recognized through timely evaluations, compensation, promotion, and other incentives.

RES Q0-2	RES QRI-10	Personnel, including partners, do not demonstrate a commitment to quality.	Low	High	Yes	The firm evaluates personal characteristics such as integrity, competence, and motivation of personnel on an ongoing basis.	RES QRe-5.01
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# Information & Communication

QO #	Ref:	Quality Objectives
I&C QO-1	QM sec. 10, par. .34a	The information system identifies, captures, processes, and maintains relevant and reliable information that supports the SOQM, whether from internal or external sources.
I&C QO-2	QM sec. 10, par. .34b	The culture of the firm recognizes and reinforces the responsibility of personnel to exchange information with the firm and with one another.
I&C QO-3	QM sec. 10, par. .34c	<p>Relevant and reliable information is exchanged throughout the firm and with engagement teams, including the following:</p> <ul style="list-style-type: none"> <li>i. Information is communicated to personnel and engagement teams, and the nature, timing, and extent of the information is sufficient to enable them to understand and carry out their responsibilities relating to performing activities within the SOQM or engagements.</li> <li>ii. Personnel and engagement teams communicate information to the firm when performing activities within the SOQM or engagements.</li> </ul>
I&C QO-4	QM sec. 10, par. .34d	<p>Relevant and reliable information is communicated to external parties, including the following:</p> <ul style="list-style-type: none"> <li>i. Information is communicated by the firm to or within the firm's network or to service providers, if any, enabling the network or service providers to fulfill their responsibilities relating to the network requirements or network services or resources provided by them.</li> <li>ii. Information is communicated externally when required by law, regulation, or professional standards or to support external parties' understanding of the SOQM.</li> </ul>

# Information & Communication

## I&C QO-1

The information system identifies, captures, processes, and maintains relevant and reliable information that supports the system of quality management, whether from internal or external sources.

QO#	QRi #	Quality Risk	Likelihood	Impact	Quality Risk	Quality Response	QRe#
I&C QO-1	I&C QRi-11	The firm fails to identify a requirement to communicate with an external party.	Low	High	Yes	The firm communicates information externally when required by law, regulation, or professional standards. For example, if the firm becomes aware of noncompliance with laws and regulations by a client, and relevant ethical requirements require the firm to report the noncompliance to an appropriate external authority.	I&C QRe-1.02

## I&C QO-4

Relevant and reliable information is communicated to external parties, including the following:

- Information is communicated by the firm to or within the firm's network or to service providers, if any, enabling the network or service providers to fulfill their responsibilities relating to the network requirements or network services or resources provided by them.
- Information is communicated externally when required by law, regulation, or professional standards or to support external parties' understanding of the system of quality management.

## I&C QO-4

## I&C QRi-53

Information is not communicated externally when required by law, regulation, or professional standards, or to support external parties' understanding of the SOQM.

Medium

High

Yes

The firm communicates information about our SOQM as prescribed by our policies and procedures with the following external parties if requested:

- Management or those charged with governance of a potential new client
- External oversight authorities
- Group auditors or other users of the firm's engagement reports

I&C QRe-1

# Risk Assessment example 1

- ▶ Component
  - Governance and Leadership
- ▶ Quality Objective
  - Leadership demonstrates a commitment to quality through its actions and behaviors
- ▶ Quality Risk
  - Professionals in leadership positions prioritize economic gain over quality through their actions and behaviors
- ▶ Response to Quality Risk



# Risk Assessment example 1

- ▶ Response to Quality Risk
  - ▶ A. Policies are in place to prohibit placing economic gain over quality. Leadership is evaluated annually, and standardized evaluations prioritize quality over financial and operational metrics
  - ▶ B. Engagement partners are required to review and sign off on acceptance and continuation procedures documentation for high-risk engagements

# Risk Assessment example 1

- ▶ Component
  - Governance and Leadership
- ▶ Quality Objective
  - Leadership demonstrates a commitment to quality through its actions and behaviors
- ▶ Quality Risk
  - Professionals in leadership positions prioritize economic gain over quality through their actions and behaviors
- ▶ Response to Quality Risk
  - A. Policies are in place to prohibit placing economic gain over quality...

# Risk Assessment example 2

- ▶ Component
  - Relevant ethical requirements
- ▶ Quality Objective
  - The firm/organization and its personnel understand the relevant ethical requirements to which the firm/organization and firm/organization's engagements are subject and fulfill their responsibilities in relation to such requirements
- ▶ Quality Risks
  - The firm/organization and its personnel fail to fulfill their responsibilities in relation to the relevant ethical requirements to which the firm/organization and the firm/organization's engagements are subject
- ▶ Response to Quality Risk

# Risk Assessment example 2

- ▶ Response to Quality Risk
- ▶ A. The firm/organization obtains written confirmation, upon hire and at least annually, of compliance with its policies and procedures regarding relevant ethical requirements from all required personnel
- ▶ B. The firm/organization requires sufficiently experienced engagement team members to identify matters for consultation or consideration during the engagement

# Risk Assessment example 2

- ▶ Component
  - Relevant ethical requirements
- ▶ Quality Objective
  - The firm/organization and its personnel understand the relevant ethical requirements to which the firm/organization and firm/organization's engagements are subject and fulfill their responsibilities in relation to such requirements
- ▶ Quality Risks
  - The firm/organization and its personnel fail to fulfill their responsibilities in relation to the relevant ethical requirements to which the firm/organization and the firm/organization's engagements are subject
- ▶ Response to Quality Risk
  - The firm/organization obtains written confirmation, upon hire and at least annually, of compliance with its policies and procedures regarding relevant ethical requirements from all required personnel

# Risk Assessment example 3

- ▶ Component
  - Acceptance and Continuance of Client engagements
- ▶ Quality Objective
  - The financial and operational priorities of the firm/organization do not lead to inappropriate judgments about whether to accept or continue a client relationship or specific engagement
- ▶ Quality Risk
  - An engagement partner makes inappropriate judgments about whether to accept or continue a client relationship or specific engagement based on financial and operational priorities
- ▶ Response to Quality Risk

# Risk Assessment example 3

- ▶ Response to Quality Risk
- ▶ A. Policies are in place to prohibit a firm/organization from accepting or continuing a client relationship based on inappropriate financial and operational priorities. A newly developed, standardized acceptance and continuance form is now completed, and all engagements requiring an EQR must also have EQR sign off on the form prior to commencement of the engagement
- ▶ B. Leadership promotes a culture where collaboration and open communication are encouraged. Quarterly surveys are sent to all personnel to gauge the firm/organization's culture

# Risk Assessment example 3

- ▶ Component
  - Acceptance and Continuance of Client engagements
- ▶ Quality Objective
  - The financial and operational priorities of the firm/organization do not lead to inappropriate judgments about whether to accept or continue a client relationship or specific engagement
- ▶ Quality Risk
  - An engagement partner makes inappropriate judgments about whether to accept or continue a client relationship or specific engagement based on financial and operational priorities
- ▶ Response to Quality Risk
  - A. Policies are in place to prohibit a firm/organization from accepting or continuing a client relationship based on inappropriate financial or operational priorities...



# Risk Assessment example 4

- ▶ Component
  - Engagement performance
- ▶ Quality Objective
  - Engagement documentation is assembled on a timely basis after the date of the engagement report, and is appropriately maintained and retained
- ▶ Quality Risk
  - Engagement documentation is not assembled on a timely basis after the date of the engagement report or is not appropriately maintained and retained
- ▶ Response to Quality Risk

# Risk Assessment example 4

- ▶ Response to Quality Risk
- ▶ A. Final engagement files are assembled by the earlier of time limits required by professional standards and applicable regulatory requirements, if any, or 60 days from the report release date. The Quality Partner will review a master list of client engagements every quarter for compliance
- ▶ B. The firm/organization provides personnel with the firm/organization's practice aids that prescribe the factors the engagement team should consider in the planning process and the extent of documentation of those considerations

# Risk Assessment example 4

- ▶ Component
  - Engagement performance
- ▶ Quality Objective
  - Engagement documentation is assembled on a timely basis after the date of the engagement report, and is appropriately maintained and retained
- ▶ Quality Risk
  - Engagement documentation is not assembled on a timely basis after the date of the engagement report or is not appropriately maintained and retained
- ▶ Response to Quality Risk
- ▶ A. Final engagement files are assembled by the earlier of time limits required by professional standards and applicable regulatory requirements, if any, or 60 days from the report release date....

# Risk Assessment example 5

- ▶ Component
  - Resources
- ▶ Quality Objective
  - Personnel are hired, developed, and retained and have the competence and capabilities to consistently perform quality engagements, including having knowledge or experience relevant to the engagements the firm/organization performs, and specifically government audits and employee benefit plans
  - Quality Risk
    - Personnel do not have the appropriate continuing professional education required by Generally Accepted Government Audit Standards (GAGAS) or by AICPA Employee Benefit Plan Audit Quality Center requirements (EBPAQC)
  - Response to Quality Risk

# Risk Assessment example 5

- ▶ Response to Quality Risk
- ▶ A. Individuals who will be interviewing candidates or otherwise participating in the hiring process are trained in interviewing techniques
- ▶ B. The firm/organization has a policy that all audit personnel obtain at least 4–8 CPE credits per calendar quarter related to both governmental and EBP auditing and accounting through self-study courses, webcasts, annual updates, conferences, the Frank and Chris show, etc... This will be tracked through a new CPE digital tracking system and monitored quarterly by the firm/organization's newly designated CPE administrator

# Risk Assessment example 5

- ▶ Component
  - Resources
- ▶ Quality Objective
  - Personnel are hired, developed, and retained and have the competence and capabilities to consistently perform quality engagements, including having knowledge or experience relevant to the engagements the firm/organization performs, and specifically government audits and employee benefit plans
  - Quality Risk
    - Personnel do not have the appropriate continuing professional education required by Generally Accepted Government Audit Standards (GAGAS) or by AICPA Employee Benefit Plan Audit Quality Center requirements (EBPAQC)
  - Response to Quality Risk
    - B. The firm has a policy that all audit personnel obtain 4–8 CPE credits per calendar quarter related to both governmental and EBP auditing and accounting through....

# Information and Communication

- ▶ Relevant and reliable information needed to operate the SQM
- ▶ Continuous flow of information embedded in firm culture and driven from top leadership
- ▶ Establish information system
- ▶ Transparency to external parties
- ▶ Expected continual innovation

# What's not new, but has changed?



# Other key changes

- ▶ Governance and Leadership
  - Focus on culture that demonstrates commitment to quality
  - Organizational structure and assignment of roles, responsibilities and authority
- ▶ Relevant ethical requirements
  - Emphasis on the responsibilities of all relevant ethical requirements, including independence
  - Encompasses network firms and service providers

# Other key changes, cont.

## ▶ Acceptance and Continuance

- Emphasis on ability to perform an engagement in accordance with professional standards
- Integrity and ethical values of the client
- Firm competencies and capabilities
- No undue influence of financial and operational priorities

# Other key changes, cont.

- ▶ Engagement Performance
  - Engagement partner ultimately responsible and continuous involvement
  - Supervision, professional judgment, professional skepticism considerations
  - Requirements related to EQR moved to SQMS No. 2

# Other key changes, cont.

## ► Resources

- Focus changed from “Human Resources” to “Resources”
- Includes human, technological and intellectual resources used in the system and performing engagements
- Obtaining, developing, using, maintaining, allocating, and assigning all resources (including financial)
- Accountability of personnel and commitment to quality
- New requirement that firms hire, develop, and retain personnel with the competence and capabilities to perform activities or carry out responsibilities within the SQM
- New requirement that firms obtain individuals from external sources (e.g., a network firm, another network, or a service provider) when the firm does not have sufficient or appropriate personnel to operate the SQM or perform engagements

# Other key changes, cont.

- ▶ Monitoring and Remediation
  - Tailor monitoring activities
  - Framework for evaluating findings including assessment of root causes

# SQMS No. 2, Engagement Quality Reviews

- ▶ An EQR as a response to quality risk for any type of engagement – not just audits
- ▶ Emphasizes the importance of an EQR
- ▶ Enhances robustness of eligibility of EQR's (whether internal or external) as well as the performance and documentation of an EQR
- ▶ More clearly differentiates the responsibilities of the Firm vs the EQR

# SQMS No. 2, Engagement Quality Reviews

## ▶ Some Uniqueness

- EQR – Objective Evaluation
  - They are not a member of the engagement team
- Firm est. criteria for eligibility
  - Competence/capabilities/time/appropriate authority
  - Comply with ethical requirements/including independence
  - Comply with laws and regs applicable to the EQR
  - Previous Engagement – served as Eng. Partner
    - Cooling off period (application guidance)

# Other Quality Management Standards

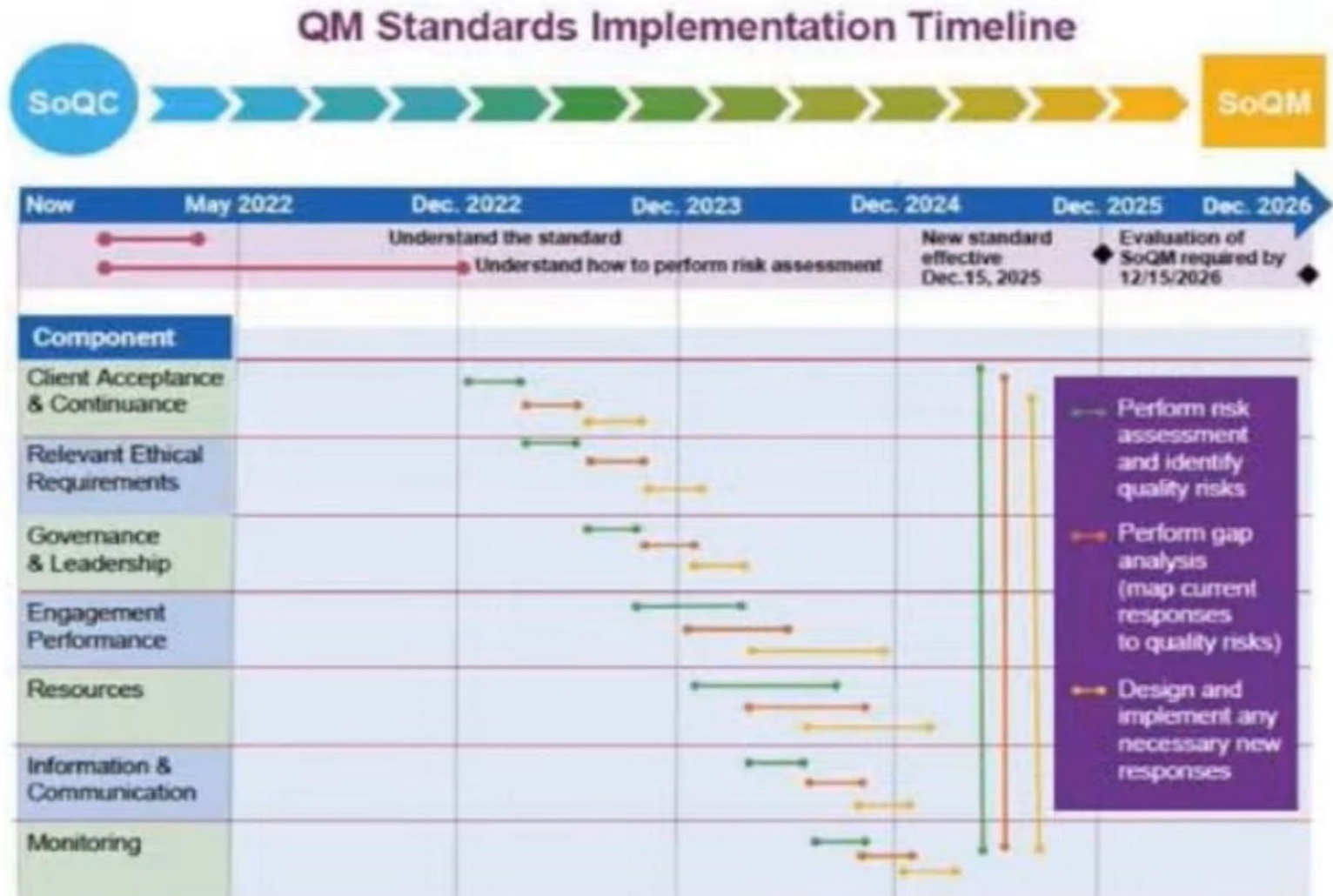
- ▶ *SAS 146, Quality Management for an Engagement Conducted in Accordance with Generally Accepted Auditing Standards*
  - Updates and supersedes AU-C section 220 and addresses quality management at the engagement level, focusing on the quality responsibilities of the engagement team and engagement partner



# Other Quality Management Standards

- ▶ SSARS 26, Quality Management for an Engagement Conducted in Accordance with Statements on Standards for Accounting and Review Services
  - Amends the SSARSs to conform with SQMS Nos. 1 and 2

# Implementation timeline



# Take Action

- ▶ Understand the standards
  - Executive summaries
  - Crosswalks
  - Webcasts
  - Practice aids
  - CPE courses
- ▶ Develop Implementation plan
  - Ownership and leadership
  - Identify resources
  - Talk with peer reviewer
  - Develop timeline

# Take Action, cont.

- ▶ Perform risk assessment
  - Establish quality objectives
  - Identify and assess quality risks
- ▶ Perform gap analysis and design and implement responses
  - Map responses to quality risks
- ▶ Prepare documentation
  - Will likely differ depending on complexity
  - As complexity increases, may need more granular documentation

# Take Action, cont.

- ▶ Establish process for ongoing monitoring and remediation
  - Consider various factors when establishing monitoring activities
- ▶ Evaluate new system
  - Evaluate within one year of December 15, 2025, and annually thereafter
  - Required to evaluate even in a peer review year

# Documentation



- ▶ Support a consistent understand of the System by personnel
- ▶ Support consistent implementation & operation of responses
- ▶ Evidence of design, Implementation & operation
  - By individual or individuals responsible/accountable for the System.

# Documentation

## ► Considerations:

- Identify individual/individuals assigned responsibility for the system
- Quality objectives and quality risks
- Responses to address qr
- Monitoring & remediation
  - Evidence of monitoring
    - Required Min. Annual
    - Eval of findings/Identification & ROOT CAUSE
    - Remedial actions to address
    - Conclusion reached
      - Don't forget SQMS 2

# Documentation

- ▶ Evidence of Compliance with SQMS
  - Formal
    - Manuals, Checklist, Forms
  - Informal
    - Emails, Website postings
  - Form and content varying (IT applications, databases)
  - Documentation Scalable –
    - Larger/Complex 
    - Smaller/Less complex 



# Questions?