

Audit & Assurance Alert

CANADIAN STANDARDS ON QUALITY CONTROL AND CANADIAN AUDITING STANDARDS

APRIL 2019

Exposure Draft on Quality Management

The purpose of this *Audit & Assurance Alert* is to raise awareness of the [recent Exposure Draft approved by the Auditing and Assurance Standards Board \(AASB\)](#) in January 2019 and issued on April 5, 2019, highlighting significant changes to managing quality at the firm and engagement level.

The International Auditing and Assurance Standards Board (IAASB) issued four Exposure Drafts in February 2019 including:

- overall Explanatory Memorandum, *The IAASB's Exposure Drafts for Quality Management at the Firm and Engagement Level, Including Engagement Quality Reviews*
- proposed International Standard on Quality Management (ISQM) (formerly International Standard on Quality Control (ISQC 1)) 1, *Quality Management for Firms that Perform Audits or Reviews of Financial Statements, or Other Assurance or Related Services Engagements*
- proposed new International Standard on Quality Management (ISQM) 2, *Engagement Quality Reviews*
- proposed International Standard on Auditing (ISA) 220 (Revised), *Quality Management for an Audit of Financial Statements*

The AASB adopts ISQMs as Canadian Standards on Quality Management (CSQMs) and ISAs as Canadian Auditing Standards (CASs). Therefore, the AASB's exposure draft mirrors that of ISQM 1, ISQM 2 and ISA 220, with additional Canadian-specific questions.

Why Should I Read the Exposure Draft?

The Exposure Draft affects all practitioners because it proposes significant changes to the foundational quality control standards at the firm and engagement level.

The scope of extant CSQC 1 does not apply to related services in Canada. The AASB is proposing to adopt ISQM 1 as CSQM 1, therefore, it would apply to all standards in the *CPA Canada Handbook – Assurance (the Handbook)*, including related services engagements. Related services engagements in the *Handbook* include:

- compilation engagements (Section 9200¹)
- agreed-upon procedures engagements (Section 9100² and 9110³)
- engagements to report on supplementary matters arising from an audit or a review engagement (CSRS 4460⁴)

The AASB is proposing not to retain the narrower scope of CSQC 1 for the following reasons:

- It is in the public interest that practitioners consistently perform high-quality engagements. A system of quality management will support the consistent performance of high-quality engagements.
- Related services engagements are being conducted for a broader range of external users. They are relevant and sought-after services. As a result, there is an increased need for quality management standards to drive the consistent performance of high-quality engagements.
- Proposed ISQM 1 is designed to accommodate different firms, engagements and subject matters now and in the future. It is intended to be proportionate to the nature of the firm and the engagements it undertakes, while requiring a base level of quality management. As a result, the standard will facilitate the application of systems of quality management to smaller firms, including firms that only conduct related services engagements.

Expanding the scope of the Canadian quality management standards to include related services engagements represents a significant change for smaller firms and sole practitioners that do not currently apply CSQC 1.

Canadian practitioners have an ability to influence the development of the ISQMs and ISAs so the standards will be clear and understandable, and can be practically applied to audits in Canada (e.g., are the proposals scalable for audits of less complex entities?). Practitioners are strongly encouraged to read the IAASB's Exposure Drafts, in addition to the AASB's Exposure Draft, to familiarize themselves with the proposed changes and to consider and provide feedback directly to the AASB and the IAASB on how these changes will be applied in practice.

1 *Compilation Engagements*, Section 9200

2 *Reports on the Results of Applying Specified Auditing Procedures to Financial Information Other Than Financial Statements*, Section 9100

3 *Agreed-Upon Procedures Regarding Internal Control Over Financial Reporting*, Section 9110

4 Canadian Standard on Related Services (CSRS) 4460, *Reports on Supplementary Matters Arising from an Audit or a Review Engagement*

What Is the Deadline for Providing Comments?

The AASB must receive all comments by **June 7, 2019**.

The IAASB must receive all comments by **July 1, 2019**.

If you would like the AASB to consider your response letter when drafting its own response to the IAASB's Exposure Drafts, please submit it as early as possible.

What Is Included in the Exposure Draft and Where Can You Find It?

The Exposure Draft consists of:

- a summary of proposals
- key public interest considerations
- a discussion of proposed significant Canadian amendments
- a discussion of the proposed scope of CSQM 1
- a discussion of conforming and consequential amendments
- a link to the IAASB's Exposure Drafts, including its Explanatory Memorandums
- a description of the AASB's process for adopting ISQMs and ISAs
- a proposed effective date

The [Exposure Draft](#), including a list of questions for practitioners, can be found online.

What Are the Proposed Changes to the Quality Management Standards?

The IAASB's Exposure Drafts propose several key changes to managing quality at the firm and engagement level. The following discussion summarizes key aspects of the IAASB's proposals.

ISQM 1

Proposed ISQM 1 deals with a firm's responsibilities to design, implement and operate a system of quality management for audits or reviews of financial statements, or other assurance or related services engagements. Proposed ISQM 1 takes a risk-based, proactive approach to managing quality at the firm and engagement level. The new approach, termed, quality management, focuses the firm's attention on risks that may have an impact on engagement quality. It requires the firm to transition from policies and procedures that address standalone elements, as required by extant ISQC 1, to an integrated approach that reflects the system of quality management as a whole.

Applying a risk-based approach to the design, implementation and operation of the system of quality management, allows a firm to take into account:

- the nature and circumstances of the firm, including whether it is part of a network or uses service providers or other internal or external factors
- the nature and circumstances of the engagements performed by the firm (i.e., although the firm is responsible for establishing its system of quality management, aspects of the system of quality management may be implemented at the engagement level)

Accordingly, the complexity and formality of firms' systems of quality management will vary.

ISQM 2

The IAASB recognizes that engagement quality reviews support the exercise of professional skepticism at the engagement level by providing an objective evaluation of engagement teams' significant judgments made in performing an engagement. Given the importance of engagement quality reviews in the overall context of quality management, the IAASB developed a separate standard, ISQM 2.

Proposed ISQM 2 is a new standard that deals with:

- the appointment and eligibility of the engagement quality reviewer
- the engagement quality reviewer's responsibilities relating to performing and documenting an engagement quality review

Having a separate standard for engagement quality reviews supports scalability of the quality management standards. In circumstances when a firm determines that there are no engagements for which an engagement quality review should be performed, there is no need to refer to the requirements of ISQM 2.

ISA 220

Proposed ISA 220 deals with the specific responsibilities of the auditor regarding quality management at the engagement level for an audit of financial statements, and the related responsibilities of the engagement partner. Requirements have been revised to:

- Clarify the role and responsibilities of the engagement partner, particularly the required involvement of the engagement partner throughout the audit engagement.
- Emphasize it is the engagement partner's responsibility for managing and achieving quality at the engagement level.
- Emphasize the importance of the application of appropriate professional judgment and exercise of professional skepticism throughout the audit engagement.
- Modernize ISA 220 for the evolving environment, including changes to audit delivery models and the use of technology in the audit.

Proposed ISA 220 is meant to be scalable for firms of different sizes and for engagements where the nature and circumstances differ.

Other Resources

1. **Overall Explanatory Memorandum:** [The IAASB's Exposure Drafts for Quality Management at the Firm and Engagement Level, Including Engagement Quality Reviews](#)
2. **Exposure Draft:** [Proposed International Standard on Quality Management 1 \(Previously International Standard on Quality Control 1\)](#), *Quality Management for Firms that Perform Audits or Reviews of Financial Statements, or Other Assurance or Related Services Engagements*
3. [Draft Frequently Asked Questions Regarding Proposed ISQM 1](#)
4. [Draft Examples: How the nature and circumstances of the firm and the engagements it performs affect the implementation of proposed ISQM 1](#)
5. **Exposure Draft:** Proposed International Standard on Quality Management 2, [Engagement Quality Reviews](#)
6. **Exposure Draft:** Proposed International Standard on Auditing 220 (Revised), [Quality Management for an Audit of Financial Statements](#)

Comments

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